

VOL. XXX NO. 3
THIRD QUARTER
2002

The Indonesian Quarterly

CURRENT EVENTS

- The Rise of China: A Challenge for East Asia
- War against Terror: Lessons for Indonesia

REVIEW OF ECONOMIC DEVELOPMENT

- Some Concerns Over Indonesia's Economic Recovery

REVIEW OF POLITICAL DEVELOPMENT

- Indonesia's New Constitution: A Peaceful Reform

ARTICLES

- Indonesia and the September 11 Attacks:
Domestic Reactions and Implications
- Indonesia's External Trade and Competitiveness:
Assessing the Economic Costs of Terror
- OECD Standards on Money Laundering and Terrorist Financing
- Mollucan Influence on Dutch Foreign Policy
- The Indonesian Crisis from 'Krismon' to 'Kristal':
Perception of Social and Cultural Impact in Jakarta and Semarang



CENTRE FOR STRATEGIC
AND
INTERNATIONAL
STUDIES

The Quarterly

The Indonesian Quarterly is a journal of policy oriented studies published by the Centre for Strategic and International Studies (CSIS), Jalan Tanah Abang III/23-27, Jakarta 10160. It is a medium for research findings, evaluations and views of scholars, statesmen and thinkers on the Indonesian situation and its problems. It is also a medium for Indonesian views on regional and global problems. The opinions expressed in *The Indonesian Quarterly* are those of their authors and do not necessarily reflect the opinion of the CSIS.

The Logo



To better represent the underlying ideas that gave birth to the CSIS in 1971 the Centre uses as of 1989 the logo that figures on the front cover of this journal. The original, in bronze, designed by G. Sidharta, it consists of a disc with an engraving that depicts the globe which serves as a background to a naked man with an open book laid on a cloth over his lap, his left hand pointing into the book, his right hand raised upwards. Altogether it symbolises the Centre's nature as an institution where people think, learn and communicate their knowledge to whoever are interested, to share it with them, mankind the world over being their concern and the globe their horizon. The nakedness symbolises the open-mindedness, the absence of prejudice, in the attitude of the scholars who work with the Centre, just as it is with scholars everywhere. The inscription reads "*Nalar Ajar Terusan Budi*", which in the Javanese language essentially means that to think and to share knowledge are only the natural consequence of an enlightened mind. It is a *surya sengkala*, that is *chandra sengkala*, a Javanese traditional way to symbolise a memorable year in the lunar calendar, adapted to the solar calendar system. It consists in using words that express the perceived meaning of the commemorated year while marking the year at the same time, each word having a numerical value. Thus, the inscription, in reverse order, represents the year the CSIS was established: 1971.

Editor

Bantarto Bandoro

Advisory Board of Editors

Mari Pangestu, Hadi Soesastro, J. Kristiadi, Rizal Sukma, T.A. Legowo, Medelina K. Hendityo, Pande Radja Silalahi, Tubagus Feridhanusetyawan.

SIT

01381/SK/Dirjen PG/SIT/72

ISSN

0304-2170

The Indonesian Quarterly

VOL. XXX NO. 3
THIRD QUARTER,
2002

CONTENTS

ABSTRACTS

222

CURRENT EVENTS

- The Rise of China: A Challenge for East Asia
Jusuf Wanandi

224

- War against Terror: Lessons for Indonesia
Bantarto Bando

234

REVIEW OF ECONOMIC DEVELOPMENT

- Some Concerns Over Indonesia's Economic Recovery
Staff, Department of Economics, CSIS

237

REVIEW OF POLITICAL DEVELOPMENT

- Indonesia's New Constitution: A Peaceful Reform
Staff, Department of Politics and Social Change, CSIS

252

ARTICLES

- Indonesia and the September 11 Attacks:
Domestic Reactions and Implications
Rizal Sukma

263

- Indonesia's External Trade and Competitiveness:
Assessing the Economic Costs of Terror
William E. James

279

- OECD Standards on Money Laundering and Terrorist Financing
Jerry W. Rowe

293

- Mollucan Influence on Dutch Foreign Policy
Robert Aspeslagh

306

- The Indonesian Crisis from 'Krismon' to 'Kristal': Perceptions of Social
and Cultural Impact in Jakarta and Semarang
Yasmin Sungkar

327

ABSTRACTS

INDONESIA AND THE SEPTEMBER 11 ATTACKS: DOMESTIC REACTIONS AND IMPLICATIONS

By Rizal Sukma

The impacts of the September 11 attacks felt accross the globe and it reinforced the notion of the borderless world. Indonesia faced with an formidable challenge in handling the impacts of the event on its domestic scene. As the largest Muslim country in the world, Indonesia's reaction to the September attacks and the subsequent American-led war on terrorism would certainly not be lost on the US and on the international community. The article analyzes the reaction of Indonesia to the September 11 attacks. The event of September 11 not only posed serious challenge to President Megawati since it took office| in July 2001, but also demonstrate the new dynamics within Indonesia Islamic community and reinforced the importance of Islam factor in domestic politics.

INDONESIA'S EXTERNAL TRADE AND COMPETITIVENESS: ASSESSING THE ECONOMIC COSTS OF TERROR

By William E. James

This article attempts to qualitatively assess how the September 11 attacks and related events may have influenced the external trade and competitiveness of Indonesia using the most recent available data. It also identifies challenges facing Indonesia and the implication of Indonesia's stance on the fight against terrorism. The author argues that there is little doubt that the September 11 attacks have had a negative impact on Indonesia's trade and competitive position. The fact that recession had already begun in both of Indonesia's major export markets -USA and Japan- before the attacks ocured make it extremely difficult to infer the extent to which each of these events is to be blame for the subsequent downturn in export and imports.

OECD STANDARDS ON MONEY LAUNDERING AND TERRORIST FINANCING

By Jerry W. Rowe

Money laundering is organized crime's way of trying to disprove the adage that "crime doesn't pay". It is an attempt to assure drug dealers, illegal arms dealers, corrupt public officials and other criminals that they can hide their profits and to provide them the fuel to operate and expand their ciminal enterprises. In an attempt to combat money laundering, the People's Legislative Assembly of Indonesia enacted a money laundering law which incorporate many of the recommendations that have been developed and issued by the Financial Action Task Force (FATF). The article discusses the recommendation of FATF and offers insight into the next phase of combatting money laundering and terrorist financing in Indonesia.

MOLUCCAN INFLUENCE ON DUTCH FOREIGN POLICY

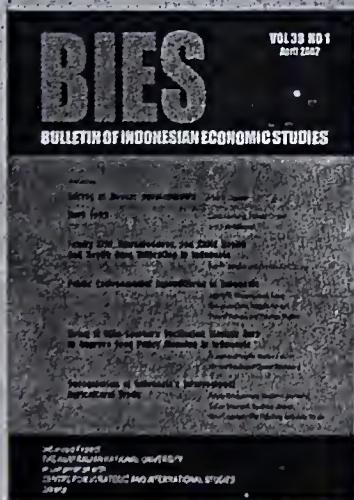
By Robert Aşpeslagh

This article discusses two periods in the history of the Moluccan community in the Netherlands. The first periods deals with the violent actions of the Molluccans in the Netherlands during the Seventies and their consequences for Dutch foreign policy in Indonesia. The second deals with the atrocities in the Moluccans during the change over from the 20th century into the new Millennium and their influence on Dutch foreign policy toward Indonesia. Both periods of internal and external violence with regards to the Netherlands will be compared in the light of different political situation in Indonesia and changed position of the Moluccan community in the Netherlands.

THE INDONESIAN CRISIS FROM 'KRISMON' TO 'KRISTAL': PERCEPTIONS OF SOCIAL AND CULTURAL IMPACT IN JAKARTA AND SEMARANG

By Yaşmin Sungkar

This article studies how and to what extent people are effected by economic problems and captures a detailed picture of people's perception of various issues such as the economic condition of their personal life and their nation in general and their government's policy in handling the crisis. The author concluded that the monetary crisis has seriously impacted the economic as well as the social, culture and political life of Indonesia. The impact of the crisis on social-cultural aspect of national and development still persist and will require years to address.



The *Bulletin of Indonesian Economic Studies* (BIES) is a peer-reviewed journal published by the Indonesia Project, The Australian National University.

The journal fills a significant void by providing a well respected outlet for quality research on the Indonesian economy and related fields such as law, the environment, demography, education and health. In doing so, it has played an important role since 1965 in helping the world, and Indonesians themselves, to understand Indonesia. In addition to papers reporting economic analysis and research, each issue leads with a 'Survey of Recent Developments', which aims to be accessible to non-economists, and helps to account for the journal's diverse readership within academia, government, business and the broader public.

The BIES is published three times a year, in April, August and December and is available in Indonesia from CENTRE FOR STRATEGIC AND INTERNATIONAL STUDIES, Jalan Tanah Abang III/23-27, Jakarta 10160, at Rp 85.000,00 per year, Rp 30.000,00 per issue.

Payment should be sent to Rupiah Account No. 0018.01.000211.30.1, BRI Cabang Tanah Abang, Jakarta 10160.

CURRENT EVENTS

The Rise of China: A Challenge for East Asia

Jusuf Wanandi

CHINA'S CURRENT DEVELOPMENT

THE biggest challenge for East Asia in the longer term is the China's rise as a great power in 20 or 30 years time. Even if economies do not forever grow in a linear line upwards as the East Asian crisis of 1997 has shown, China will still be a great power in the next 40-50 years. Only great political calamities, such as the Great Leap Forward in 1958-1962 or the Cultural Revolution in 1966-1976, could give real set-back with dire consequences to China. At this point, a political crisis could create some instabilities, which may curb her economic development.

While the political system and leaders could at present try to resist change, it becomes a natural development for a fast changing society such as China, because the economic development has been running fast and for a long period of time. Such a development has created a critical middle-class group who demand some-

thing more than mere economic development. But, if handled appropriately, namely by opening the political system gradually, it should not become a calamity or a deep crisis. In China, the economic development and individual freedoms have improved dramatically since 1979, when liberalization of the economy started. In this case, she apparently had enough reserves in the economy and some flexibility in the political system. Whether that is adequate, however, should yet be seen in the next few years. But as East Asian countries, especially Indonesia, have experienced since the crisis of 1997, China will always need some corrections after undergoing long-term development, and for further development some flexibility and openness of the political system are imperative.

CHALLENGES FOR CHINA

For China alone the challenges are huge because of the country's magnitude with a population of 1.3 billion people. With such a large size,

the problems also become huge, albeit not insurmountable. The problems of discrepancies in economic development between over 300 million people in the coastal part which are considered middle income people, and almost 1 billion in the inner parts of China which are considered low income people, are real and vast. In the coastal part the economy might look as NIE's, with per capita income of US\$2000 - 3000 per annum has been achieved, while people in the inland part may only have a per capita of US\$600 - 800 annually.

In addition to the problem of economic inequality that China has to face, the restructuring of the banking system and the SOE have not been going very smoothly and the pace has slowed down due to the threat from unemployment that is most likely to increase by another 50-100 million people on top of the existing 200 millions plus. Besides, the effects of WTO membership in the medium term might not be very clear at present, because the rules that has to be introduced will only be completed and in place after a + 5-7 years of transition. Although it will hurt China on the one hand, because she has to abide to the rules of the WTO, she on the other also will become more competitive at the same time.

Another challenge for China is the governance problem. The same as in most of East Asian countries, transparency, judicial and legal system, and accountability are not China's

strength. Therefore, corruption has been high and inefficiency is very real. If fast growth of the economy could be maintained then all the changes are not going to hurt so much. But if the economy is going to slow down, then the impact of change, including because of the WTO will be much greater.

How political change is going to impact on China's development remains a big question. As experienced by other East Asian countries, China can hardly escape the fact that after a period of 20 years or so of quick and steady growth of 7-9 percent annually, a correction is bound to happen, especially if a full open economy is going to be established (including in the financial field). As a WTO member, all what China has to do is to open its economy gradually in the next 5 to 7 years. If China is wise, it will learn from the experiences of other East Asian countries, also on the sequencing of the opening of the economy. In so doing she can control the pace of change especially of the financial system, which could really be a critical factor for macro-economic stability. Second, a fast economic growth of 2 decades or so will change the society, and the country will have a larger base of middle class people, who will be pushing for political reforms.

This will put the pressures on the government to open up the political system and make it more flexible. This may not be transformed into a full-

fledged democracy immediately, but definitely a more open system that now is being practiced in China. China must have those changes in place in the next 5-10 years. Without them, the system is going to deteriorate and changes might come suddenly paired with dangerous instabilities, like in Indonesia.

This could create dramatic challenges to the existing political system. Some studies and proposals by the party and CASS (Chinese Academy of Social Sciences) have been made in order to be able to exactly make the political system more open. Although the studies and the proposals are realistic and quite courageous, it yet has to be seen whether the existing leadership is united and also as courageous to recognize the problems and the need for change and above all are willing to implement them.

What the Party tried to do at the village level with elections of some officials has not been satisfying, because it was not done consistently while the change in fact was very limited. Although at this stage every adult above 40 has still some trauma of the miseries of the cultural revolution, a younger generation is growing, which has not had the bad experiences, and therefore are more willing to push for political development and political change in the future.

So, the challenge on the political front is real, although at this stage there is no worry about a collapse of the system or of the country being split in several states. But these pressures have to be

addressed and changes have to be brought into the political system, before further developments, including economic ones, are guaranteed to be successful.

CHINA'S STRATEGIC POSITION

The East Asian region has an absolute interest to see China to succeed, because she is too important to the region in every sense. Besides, the region will be much more worst off if China is going into a crisis and damage the region again, after such a devastating crisis since 1997. If China is going to develop steadily and could overcome a mild political or economic crisis in a positive way, which is one scenario that might have a probability to happen, what are the strategic and economic challenges to the East Asian region particularly and the world generally?

In strategic terms, China is going to become the challenge for East Asia. Hence, the main question is: what is China going to do if she is going to become a great power in her own right, due to her economic and military might in 20-30 years to come? Is China going to become a new threat to the region, because she is going to reject the *status quo* with its rules and institutions or is she going to adjust and be part of the global and regional system? If for signing treaties and international rules, global and regional, as well as participating in international and regional institutions, are considered to be the criteria, then China is a *status quo* power and not a revolutionary

one, challenging existing rules and institutions.

But there is a new element coming into the strategic picture, which might have consequences for China's role and challenges in the future as a great power. That is the emerging new strategic development and new alignments due to the terrorist barbaric attack on September 11 against the USA and the reactions it has brought to the world, particularly to the Asia Pacific region. It has made the USA to change its perceptions on how world order is going to be, what new challenges are lying ahead, and how new alignments and alliances are going to be developed. Admittedly, it is not clear how stable and enduring these developments and alignments are going to be. In this context, China is belonging to the group which is considered also to have serious terrorist threats from Xinjiang province particularly from Central Asia.

To face those challenges China and Russia have finalized in May the Shanghai Treaty, where four other central Asian states also participated in the efforts to fight terrorism, among others supported by Osama bin Laden and the Taliban government. China has supported the US in its anti-terrorist policies, including the military operations against Osama bin Laden and the Taliban. She also participates in the anti-terrorist "coalition" with the US, however, cautious and limited. Because of these new developments, the worry in East Asia that strategically China as

the new great power is going to become the new challenge, because of her struggle against the *status quo* as defined and protected by the US and the West, has been somewhat alleviated. But again, nothing has been cast in concrete about these new strategic alignments and developments, and therefore some speculations about what could happen even after the tragedy of September 11, could be an important exercise. Because, despite new developments in strategies and alignments, some basic character and deep problems are going to stay of the region as already can be observed in the last few months. Although the rhetorics might be somewhat different, especially on China's side.

The earlier worry was whether China is going to behave as *status quo* power, willing to abide to existing rules, norms and institutions, or is going to be an emerging assertive and revolutionary power, who is going to challenge all of that namely the rules, institutions and the existing power. As the situation develops today, it is not a forgone conclusion that China is going to be a revolutionary power. That is because she still needs a peaceful surrounding to be able to modernize herself and she could not afford any confrontations or conflicts for some time to come. This is considered the last chance for China to be modernized and to be able to cope with the challenge and burden of 1.3 billion people, one fifth of the total world population. That is why she would like to abide to existing norms, rules and institutions, al-

though a lot has been new to her especially multilateral institutions except for the UN. In all fairness —although sometimes her tone is shrill and she seems to overreact on the slightest reason (since history is still a big burden to her)— she has not been a complete spoiler of the world order and regional order, but is more opportunist even in the Security Council. It is true, that she might be slow and sometimes obstinate towards new proposals, but she always tried very hard to give a decision and, if possible, to cooperate.

Nevertheless, the Chinese are proud people and the history of their own has been so important to them. In the longer term, after 20-30 years of successful economic development and steady military built up China could still assert herself. That is why East Asia's role could be critically important to prevent such a possible confrontation between an emerging great power such as China and the leader of the *status quo*, namely the US, who has the ambition, the ideology and the political will to lead the world. Whether nationalism and China's historic role in the region as the dominant power will be pressures to do the same again in the region leaves a question mark.

THE IMPORTANCE OF MULTILATERAL INSTITUTIONS TO CHINA

What is important at this stage is that while China needs the region, she has to be involved in all kinds of global and regional regimes and their

institutions. As such she has to be embedded in them. At the end it is only natural that she needs to get herself used to such an involvement after she becomes a modern and developed country. To achieve that the Asia Pacific region wide institutions, such as APEC and the ARF (with their second track institutions such as PECC, PBEC, and CSCAP), are important especially having the US as a member. But lately the ASEAN plus three regional mechanism consisting of the ASEAN 10 plus China, Japan and Korea is becoming also important to encourage China to cooperate more closely with the region, among others because of the East Asian financial crisis.

There has been a common need to get the region's member countries act together before outsiders were willing to assist and support East Asia. Besides, China felt more comfortable with this regional mechanism, where intrusiveness into each other domestic matters will be more limited and indirect. This type of cooperation will be limited mainly to economic affairs, while political ones could only be occasionally aired if there will be a consensus. This is mainly at the request of China, because she does not completely trust multilateral efforts in the politico-security field as yet, except for the UN where she has a veto power.

ASEAN member countries, however, have a sort of special relations to China, because China needs them in case there is any attempt to isolate her in

East Asia. On the one hand, this is because the relationship between China and Japan has not been completely stabilized and although China's relation with South Korea is in an excellent state of affair, South Korea is still a US ally. On the other hand, ASEAN consists of small and medium size countries who are political-diplomatic players in the region and sometimes in the world concerning the region. Besides, they could hardly hurt China. Now China has proposed a free trade area with ASEAN to be concluded in 2010, which is a very big gesture and whose mutual benefits have to be studied seriously by ASEAN. About the South China Sea, although ASEAN has the ears of China for a peaceful resolution, it has not been used by ASEAN to do anything substantial about it, because ASEAN itself has no unified proposal about the resolution of the overlapping claims.

Nonetheless, the code of conduct has not so far been concluded by China after more than two years of ASEAN's initiative and proposal. China has not yet accepted ASEAN's initiatives and seems to have doubts about ASEAN's future capabilities after the Asian economic crisis. In this case, ASEAN should first get their act together to be effective. Second, ASEAN has to increase cooperation with the US. Because the US is the most important trading partner and investor, who has kept stability and peace in the region since World War II. The efforts to get China in-

involved in the region and becoming a *status quo* power is a long-term effort; and ASEAN has to do that with others in the East Asian region to have the same impact. Nonetheless, In the end the role of the US could be the most crucial one in relation to China's future policies, because only the US can balance China and at the same time determine whether China is going to be a *status quo* power or not in the future. In this effort to anchor China in global and regional order, at least the supporting role of ASEAN and the ASEAN plus 3 have to be included and be recognized as well.

The existing fear in the region is whether a confrontation between China and the US could become a reality. That possibility has somewhat been alleviated, due to a common threat after the tragedy of September 11. Yet, the potential is still there, because the basic problems are very real especially the problem of Taiwan. Like in the Cold War when some joint operation against the Soviet Union was possible, that possibility against terrorism could also happen. It seems that some worry remains real about cooperation on both sides. Also the Taiwan question has not been put in the backburner or concerns on human rights. Hence, at least the rethorics is less brittle and relations at the highest level have been maintained actively. For ASEAN and Indonesia these new developments are good enough, because they increase stability of the region and should be supported.

THE ECONOMIC CHALLENGE FOR CHINA

So far bilateral relations between China and Indonesia have been stable, and therefore a lot could be done if Indonesia could come up with initiatives and bring it to the attention of China. China has considered Indonesia as a leader of ASEAN and still has a high regard for it, despite the prolonged crisis it has to undergo. But Indonesia has to recognize what she could and should do with China at the regional level and at the bilateral level, because both are important and should be pursued. What is now coming to the fore in the bilateral and regional relations between China and Indonesia is the economic relations. China's economy has increased so dramatically in the last few years, while the other East Asian ones, especially Indonesia, was in the doldrums since 1977. Therefore, the challenge from China at this stage has become more economically than strategically. The economic challenge is more urgent and immediate while the strategic one is more in the medium and long-term. Immediately, however, it should be stressed that economic relations and challenges are non-zero-sum game relations, which could include challenges but also beneficial cooperation for both economies. For Indonesia, China has become a much more stronger economic and could be devastating to some sectors of the industries that are labor in-

tensive and export earners, such as textile, garment and footwear. China's economy no doubt will be mainly felt in East Asia. Her influence depends on the future of the evolution of its economic reform program, the implementation of WTO rules and agreements and on the strategic developments in East Asia and her future role.

Furthermore, it is critical for other economies, including Indonesia, to understand China's economic developments and find out how to prevent devastating competition. That means how to find niches, complementary opportunities and benefit from China's fast growing domestic markets. Over half of China's trade is with Asian partners and the most important ones are Hong Kong where China has become a leading trading partner, for Japan China is the second, for Taiwan China is the third, for Korea China is the third, and for ASEAN China is the fourth, for Australia China is the fifth trading partner.

Roughly three quarter (75%) of China's cumulative inbound FDI has come from Asian economies, and China has become the largest FDI destination for Hong Kong, Taiwan and Singapore, the second leading destination for South Korea and the leading Asian destination for Japan. At the same time, almost 80% of all FDI into East Asia last year was to China.

As could be expected, China first and foremost was competing with the

economies of Malaysia, Thailand, the Philippines and Indonesia, since they have been mostly dependent on foreign investment and technology that now have been flowing into China and do not have the ability to move up the value-added ladder rapidly. On the other hand, the displacement of export-oriented manufacturing activities from Hong Kong, Taiwan, South Korea and Singapore occurred with limited disrupting, since the decentralization of lower level manufacturing activities have helped them to enhance competitiveness and re-deploy resources to more valuable activities.

Low labor costs, flexible labor practices and foreign investment has allowed China to become the world's leading producer and exporter of garment and related products. The sector accounts for about a quarter of China's exports, a seventh of industrial employment, and 6% of total industrial output. They have also expanded production to all garments and price points. And that has been achieved despite its access to major markets. Once China joins the WTO, it will be eligible for more favorable treatment and becomes much more competitive.

According to the US International Trade Commission, China's share of the US clothing market could increase by 20 percentage points (to more than 30%) and that of the world clothing market by more than 6 percentage points (to roughly 38%) by 2006. And

most gains come at the expense of other Asian countries. China's vast reserve army of relatively inexpensive, highly productive labor, combined with improving infrastructure, already has caused several companies organized and controlled by Hong Kong to plan a shift of production from South East Asia to China. Such a shift could have a dramatic impact on economies using the garment industry as their first step in industrialization.

The same is happening with the electronic industry, where China will attract in the future complete production chains with low cost assembly labor, improving technical sophistication and immediate access to one of the world largest markets. Asian economies with the technical capabilities to stay ahead of China will benefit. Others that rely on foreign technology capabilities and designs, will find their positions threatened by China. But in addition to its complementary and competing role, China also will emerge as a market, an investor, and a development partner for East Asian economies.

With a population approaching 1.3 billion China's domestic market is a big attraction. Besides, inhibitions such as limitations on imports, low purchasing power, inefficient distribution, geographically fragmented markets and a host of restrictions will be mostly lifted under China's WTO agreements. New opportunities will be found initially in industries in which China's domestic

producers are inefficient or where demand remains unmet, including some manufacturing industries, agriculture, and many service industries. Although China will be a big market, but is not necessarily for all East Asian economies. Japan and South Korea will find markets for advanced components, capital goods, and infrastructure.

Hong Kong will find markets especially for its service industry. Taiwan will find markets for technology-based products. Other industries are not clear in their comparative advantage. Manufacturing is not a great advantage against Chinese, while their services might not be adequately advanced to compete. Maybe resource-based products such as oil, timber products, materials, agricultural goods, and some niche manufacturing products could be their advantage.

THE ECONOMIC ROLE OF CHINA IN THE REGION

China is becoming an important international investor. That has become very real in Hong Kong, where they have prominent positions in banking, foreign trading, and construction. Because it has been a recent phenomena, the amount is still small in comparison with the size of their economy. And they have still some constraints due to recent opening of China's economy, difficulties in obtaining capital and history of state ownership. In energy already they started big for their own

energy need and sufficiency. If they have developed international competitive companies, more will come.

China can be a partner with neighboring economies through participation in specific regional infrastructure and development programs such as the Mekong Development Project, which focuses on transportation, energy, trade, communication, and investment. China is helping to develop oil fields and pipelines in Central Asia. And future developments in Siberia will also be a real potential field for China to participate.

In sum, it could be concluded that ASEAN will face tough competition from China for export markets and investment. In the short term, ASEAN's political and economic difficulties are hurting South East Asia. In the long-term, the economic weight of North East Asia threatens to make it a sideshow. And that can even be true for Singapore. They have to accelerate the integration of their markets and domestic reforms. They have to retain portions of traditional export markets while serving growing demand for resource-based products and niche consumer goods in China.

The economies that will benefit from China are those that can penetrate growing Chinese markets, develop complementary relations with the Chinese economy, attract investment from China and create development partnerships with China.

CONCLUDING REMARKS

China is already a big influence in East Asia and will be more powerful in the future. If China can overcome in the next 5-10 years her political and economic challenges due to changes because of her dramatic economic growth and development, she is for sure becoming a great power regionally and globally in the next 20 years or so.

The strategic challenges arising from such a development will be great, especially to East Asia, namely how China is going to adjust to her status and power: a revolutionary power willing to change the international and regional system and balance of power or becoming another *status quo* power maintaining stability and peace in the region and globally. The new strategic developments and alignments due to the dramatic and tragic events of September 11, would make the outcome, especially in her relations with the US, as the only super power, more peaceful than might be expected before, although the basic issues between the US and China are huge and deep divides that are not

easy to be solved and need constant attention on both sides. However, in the meantime it will be wise for East Asia to commit China to the web of rules and institution in the region and in so doing get her long-term commitment to the *status quo*.

In the economic field, China will be an immediate competitor but also partner in the medium-term. For South East Asia, it means hard work to study the Chinese economy and its future development and preparing themselves to adjust and restructure, and particularly getting their markets integrated to have a fighting change to compete with China. China's market opens up also an opportunity especially after WTO rules make it more transparent and more rule-based. China is also becoming investor in the medium-term and partner for the region's economic development.

In any event, East Asia, particularly ASEAN, and of course Indonesia has to pay more attention to China's challenges and opportunities. They are big challenges but also good opportunities if East Asia could do their utmost.

War against Terror: Lessons for Indonesia*

Bantarto Bandoro

THE Sept. 11 terrorist attacks on the United States in which thousands of innocent lives were lost has led Indonesia and other members of the Association of Southeast Asian Nations (ASEAN) to join the American-led global war against international terrorism.

The war against terrorism will be a never ending battle as the U.S. continues to seek stronger commitment from the countries in the region, especially the Philippines, Malaysia and Indonesia, of which the latter two are considered to be the operational bases for Jemaah Islamiah, a radical Islamic group allegedly linked to al-Qaeda attempting to carve out an Islamic state.

The government of Megawati Soekarnoputri has long denied the presence of substantial terrorist networks in the archipelago - but it has taken US\$50 million from Washington to assist security forces in the antiterrorist struggle.

Indonesia's has been viewed as something of a laggard in this global war, not only by the U.S., but also even by its friends in the region, Malaysia and Singapore. Since Sept. 11 Indonesia has always

been on the U.S. international policy agenda, because it allegedly is a haven for terrorist groups. Singapore has also accused Indonesia of being a safe ground for nurturing terrorist activities.

Either independently or within the context of ASEAN Indonesia has now been integrated into an antiterrorist network. Washington believes that Indonesia could play a crucial role in ensuring that "militant Islam" does not spread and thus jeopardize regional peace and security.

But the existence of Indonesia in such networking will not automatically eliminate the already strong image held by certain members of the international community that our country is hospitable toward international terrorists. Counterterrorism experts have long insisted that Indonesia has served as both a staging area and refuge for terrorists.

Indonesia participation in the antiterrorist coalition still has to be tested as the country continues to face difficulties in arresting or detaining "radical" Indonesian Muslim leaders accused by foreign countries as having al-Qaeda connections. The government always feels it needs to convince foreign envoys of its determination to fight terrorism. But Indonesia lacks the capability to do so.

*This article was first appeared in *The Jakarta Post*, 6 September 2002.

One of the effects of Sept. 11 is that Indonesia is considering an antiterrorist law, among other things. The idea that the law be introduced to curb terrorist activities has caused strong opposition from certain sectors, arguing that the law may be used to oppress certain groups in the country. Given its controversy there are further doubts of when it will become effective.

Many in the West have attempted to link the issue of terrorism with democracy and Islam. International campaigns against global terrorism serves as a kind of wake-up call for Indonesia to start thinking of combining democracy and Islam. Perhaps, it is through such a course that Indonesia will gain more sympathy from the West, the U.S. in particular.

Indonesia is now embarking on a fragile experiment of democracy. A successful management of the process by the present and future government will make the country the third largest democracy in the world and in the Muslim world. But if the experiment fails, the country will definitely become a source of gravity for possible extremist activities, thus guaranteeing another big blow to Indonesia.

Despite appreciation from the U.S. of Indonesia's perceived seriousness in fighting terrorism, we will still be closely watched by the international community as to whether we will fully respect human rights. This is the kind of issue often linked to the role of the military.

If the Indonesian Military (TNI) is going to prevail over terrorism, they have to do it in a way that respect human dignity.

The antiterrorist campaign has paved the way to normalizing the two countries' military ties, cut three years ago because of human rights abuses. It allows aid to flow again to the military. It is not an exaggeration to say that the current antiterrorist campaign makes TNI the victor.

The plan to resume the International Military Education and Training (IMET) as well as the involvement of Indonesian officers in a counter-terrorism fellowship program, provided by the U.S., will help the TNI to improve its capability or to improve its military organization within a democratic system.

One cannot deny the importance of the military factor in combating terrorism. The TNI must therefore be extra careful in using its military assistance so as not to create the impression that they are using the aid for other purposes other than defending the nation against any possible external threats.

Critics say that providing the Indonesian Military with new arsenals and other equipment is ineffective in curbing radical groups, arguing that the U.S. should not commit violence against such groups, to prevent resistance growing even stronger.

It is unlikely that U.S. troops will set their boots on Indonesian soil as they did in the Philippines, but even without this, the actions of so-called

radical groups have already generated fears. Indonesia therefore should not also ignore the possibility of such groups serving as a kind of proxy of international militant groups linked to the al-Qaeda network. This is where Indonesia needs to have reliable intelligence networking to detect the linkage and the capability to deal with terrorist elements, and this can be accomplished only with the co-operation of other countries.

The global war on terror will be a long lasting one and the endurance of its strategy will be tested against the true commitment of the participants in

the war. The war on terror has placed Indonesia on center stage in the international policy agenda of the U.S.; and the country cannot avoid being cited as a safe haven for terrorist activities unless it is willing to show that it is not all mere talk about terrorism.

Although Foreign Minister Hassan Wirayuda has said that the country has done quite a lot since Sept. 11, the question remains as to how far Indonesia is willing to go in the war against terror, and whether Indonesia will maintain its main defense that some preachers merely sound "radical", and that they are not terrorist.



FROM THE TRENCHES

The First Year of Indonesia's Crisis of 1997/98
as Seen from the World Bank's Office in Jakarta

Written by: Lloyd R. Kenward

Published by: CSIS, Jakarta

This book provides an analysis of the first year of Indonesia's crisis taking place in 1997-1998. It is written from the perspective of someone who had the opportunity to observe the development and the impact of the crisis from a strategic position: as an economist sitting in the World Bank country office in Jakarta. The book is therefore an important contribution to the growing literature on the Indonesian economic crisis for two reasons. *First*, it provides the general audience with a readable account on the evolution of the crisis. *Second*, it also presents a detailed economic analysis for the specialized reader coming from the academic or policy making community.

The book consists of three chapters. Chapter I presents a concise account of Indonesia's economic performance prior to the crisis. Chapter II provides a very detailed chronological review of the first year of the crisis. The main lessons and conclusions that emanate from the analysis are highlighted in Chapter III.

The book serves as a good example of a comprehensive political economy approach, as it manages to put economic analysis into a proper political context. Therefore, this publication is recommended for those who are interested in Asian economic crisis in general and Indonesian economic policies in particular.

2002. 1st Ed., x + 152 pp.; 25 cm, ISBN 979-8026-74-8; Rp 40.000,00.

Some Concerns Over Indonesia's Economic Recovery

Staff, Department of Economics, CSIS

INTRODUCTION

ALTHOUGH the overall economic performance is relatively flat, there is some good news on the economy. Economic growth has been accelerating since the fourth quarter of 2001, particularly since the 9-11 tragedy. Exports steadily improve despite the overall export performance that remains weak. Inflation rate is declining to about 10% (y-o-y) and is expected to reach a single digit inflation by the end of the year; and the Rupiah is steadily ranging between Rp 8,600-9,000 per US\$. Apart from these positive developments, we have serious concerns whether the increasing growth can be sustained. The source of growth remains fragile: private consumption is leveling off, manufacturing growth is waning, export recovery is fragile, and foreign investment is disappointing. We believe that economic growth will be about 3.7% by the end of the year, which is lower than the targeted official growth of 4% in 2002.

We also have a great concern over the foundation for sustainable growth, especially the legal system. Controversial and unpredictable decisions made by the Indonesian courts are still the factors that discourage foreign investors, hence hindering the prospect of economic recovery. At the same time, investors are facing great uncertainty in the labor market, which is expected to remain for some time in the future because of the prolonged controversy over labor relation laws.

ECONOMIC GROWTH

The recent data published by the Central Board of Statistics clearly show that year-on-year economic growth is accelerating, from the lowest at 1.6% in the fourth quarter of 2001 to 3.5% in the second quarter of 2002 (Figure 1). However, in order to achieve the government's target of 4% growth this year, the economy should necessarily grow by 5.1% (y-o-y) in the second semester 2002 —

an ambitious target that will not likely be achieved considering the past experience.

From the expenditure side, the growth of private and government consumption remains high. Table 1 shows that private consumption, especially non-food consumption, remains strong at more than 12% year-on-year in the second quarter of 2002. This consumption boom is also experienced by Malaysia, Thailand and Korea but the prospect of continuing high consumption growth might be more limited in Indonesia because households and corporations have been scaling back their saving rates to maintain their standard of living and business operations. The share of private consumption in GDP ratio has gone up substantially during the crisis from about 62% of GDP in 1996 to around 70% recently. However, it remains to be seen whether or not the increasing trend will continue.

The growth of overall investment remains weak, mainly because of the poor performance of foreign investment.

On the contrary, we suspect that the growth of domestic investment might have been underestimated for two reasons. *First*, household expenditures for maintaining and repairing of dwellings are not recorded under the current data. *Second*, the gross capital formation figure might underestimate the investment activities by small-scale enterprises (SMEs). On the other hand, we assume that the changes in stock (which is the residual component in calculating the growth figures) have been over estimated.

From the production side (see Table 2), agriculture was the biggest contributor to overall growth in the second quarter of 2002 (contributing to 43.7% of total growth), followed by manufacturing (19.2%) and transportation and communication (17.6%). The adverse impact of El-Nino on agriculture turned out to be mild, at least in the first semester of this year. In contrast, the manufacturing sector has not been performing well. Its annual growth has

Table 1

ECONOMIC GROWTH BY EXPENDITURE (YEAR-ON-YEAR)

Items	2001				2002	
	Q1	Q2	Q3	Q4	Q1	Q2
Private Consumption	4.0	4.7	5.8	9.2	7.1	6.4
Of which foods	1.0	2.5	2.3	3.5	1.1	1.1
Of which non-foods	7.6	7.1	9.8	15.8	13.6	12.1
Government Consumption	6.0	4.2	11.9	11.0	8.8	9.4
Gross Fixed Capital Formation	18.9	7.7	-0.8	-7.1	-6.9	-3.7
Exports	18.4	8.0	-2.6	-12.9	-5.2	-7.1
Imports	50.7	37.2	-3.7	-29.8	-25.7	-21.6
GDP	4.8	3.8	3.1	1.6	2.2	3.5

Source: Central Board of Statistics.

Table 2

ECONOMIC GROWTH BY SECTOR OF PRODUCTION (YEAR-ON-YEAR)

Items	2001				2002	
	Q1	Q2	Q3	Q4	Q1	Q2
Agriculture	2.6	1.2	-1.2	-2.4	-1.4	6.3
Mining and Quarrying	6.8	-0.3	-2.4	-5.9	-2.3	1.8
Manufacturing	4.2	4.8	4.7	3.6	3.7	2.5
Electricity, gas and water	7.3	9.9	8.9	7.6	7.9	4.7
Construction	6.2	5.7	3.5	0.7	1.7	2.4
Trade, hotel and restaurant	6.8	5.5	5.7	2.6	3.4	3.7
Transportation & Communication	6.4	7.0	7.6	8.9	8.4	8.2
Finance	3.9	3.4	2.7	2.0	2.7	2.6
Services	1.3	1.6	2.3	2.7	1.5	0.4
GDP	4.8	3.8	3.1	1.6	2.2	3.5

Source: Central Board of Statistics.

been decelerating, from 4.8% in the second quarter last year, to 3.7% in the first quarter this year, and 2.5% in the last quarter, which was the lowest since 1999. The manufacturing sector is the largest sector in the economy, contributing to about 26% of the GDP. In this case, a weakening growth in this sector will consequently lead to slower overall growth.

In summary, Indonesia's economic growth will continue to depend on private consumption at least in the next several quarters. Under the best scenario, private consumption might be able to bring 3% growth in 2002-2003, while strong recovery in exports and investment might be able to contribute to an additional of 2% of growth. But for this year, it is clearly hard to achieve the official target of growth at 4%. At best the economy can grow by 4.5-5.0% in the second semester, producing 3.8% growth rate for the whole year. At worst it will

maintain the current growth rate of 3.5%, producing 3.2% growth rate overall by the end of the year. Overall, we forecast that the economy will grow at about 3.7% in 2002.

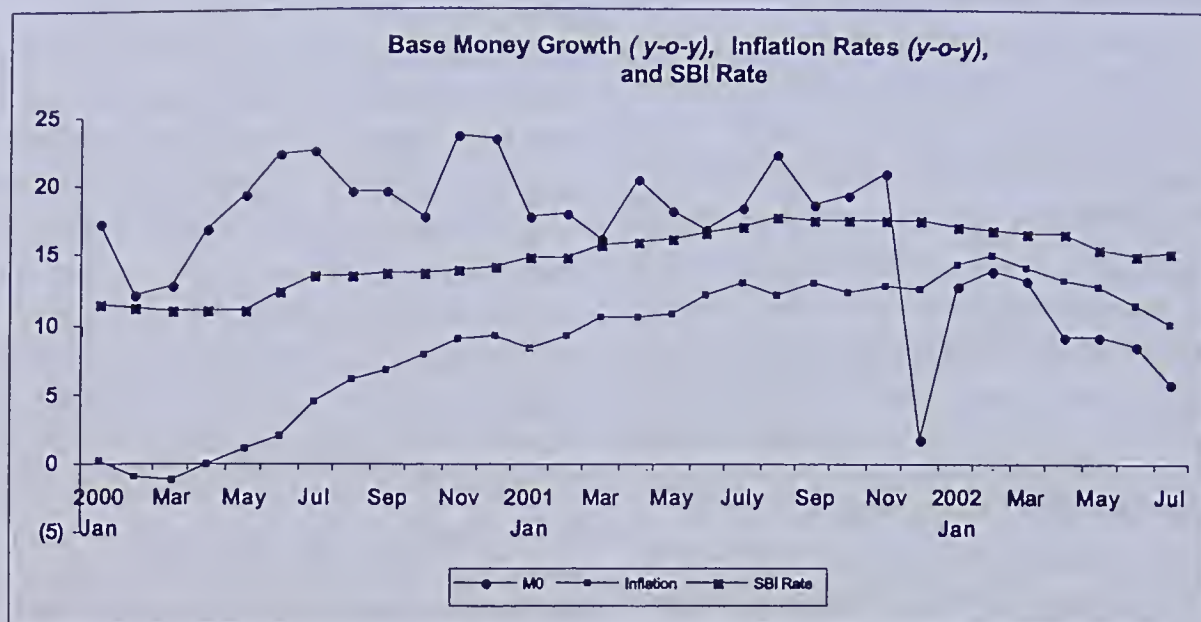
MONETARY DEVELOPMENTS

Declining Inflation and Tight Money Supply

Overall monetary indicators show that inflation is under control, as inflation rate declined from 15.1% (year-on-year) in February 2002 to 10.5% in July 2002. The prospect of having a single-digit inflation by the end of the year looks promising, taking into account the fact that this year, inflation has so far reached 5.2% (Jan-July). Our current forecast shows that single digit inflation of about 9% this year is achievable, provided that the remaining inflation from August to December would be less than 4%.

Figure 1

DECLINING BASE MONEY GROWTH AND INFLATION



In line with this declining trend, money supply remains tight. The annual growth of base money (Mo) continued to decline, from 13.3% (y-o-y) in March to 9.3 in May, and 5.9% in July, much lower than the level of growth needed to maintain single digit inflation. We estimate, based on previous experience and data, that about 11-12% annual growth of base money should be tight enough to avoid double-digit inflation. Actual base money in July (Rp 118.5 trillion) also stood below the indicative target level of Rp 125 trillion in July, or about 5% lower than the target.

The declining growth of currency in circulation is the major contributor to the decrease in overall base money growth. There is a clear indication that the demand for money, especially cash, has been declining for the last several

months, reflected by the declining both money supply and interest rate at the same time. While the decline in money demand might be a result of declining risk premium in general, we have some concern that the weakening growth of money demand is a reflection of declining economic activities in the real sectors. From the supply side, therefore, the need to have lower interest rate is clear.

Interest Rate Is Crawling Down

Because of Bank Indonesia (BI)'s initial reluctance to lower the interest rate more aggressively in order to maintain the base money growth on target, it only started to lower interest rates in July 2002. The interest rate of 1 month SBI went down from 16.6% in April to 15.2% in July, but at the same time the level of base money remained about 5% lower

than the target. Indonesia's Letter of Intent to the IMF requires Bank Indonesia to target the base money rather than the interest rate, however, recent developments suggest that BI has not been consistent in conducting monetary targeting. In other words, it has kept the tight money policy by keeping the level of base money below the target. Bank Indonesia finally allowed the SBI interest rate (1 mo.) to decline further to 14.7% in mid August, and 14.3% in the end of August. Whether or not the reduction in interest rates is enough to put the base money level back on target remains to be seen.

The recent decline of SBI rate would definitely force commercial banks to lower the deposit rate further in the near future. However, we also predict that the interest rate will remain flat in the fourth quarter because of increasing economic activities and higher inflationary pressure in towards the end of the year. The recent cut of the SBI rates would also lead to more active bond markets in the coming months. The prices of some selected government bonds, for example the ones with a fixed coupon rate of 16.5% has increased remarkably to more than 100 in mid-August. While bond prices rallied, bond yields have declined along with the declining SBI rate.

Slower Growth of Bank Credits

The flat amount of outstanding credit for the last three months reflects the slowing down of domestic investment

activities. The amount of credit channeled to the manufacturing sector has been declining rapidly, from Rp 112 trillion in February to Rp 104 trillion in June, and the declining trend seems to continue. Since March, the annual growth of manufacturing credits have entered negative territory again, and reached minus 18% (y-o-y) in June. This is consistent with the declining growth of manufacturing sector in the GDP. However, the growth of miscellaneous credits, mostly consumer credits and SME (small-medium enterprise) activities remained robust at about 35% (y-o-y). In fact, based on BI data, more than 50% of the new credits channeled by banks in June were classified as SME credits.

The Rupiah and the Stock Price

Lower inflation, slower growth of base money, improved security, lower swap premium, and higher confidence in the economy in general have set the foundation for a stable currency. The good news from Paris Club, successful divestment of BCA, and IBRA's asset sales have certainly played a major role in supporting the appreciation of the Rupiah since January this year. But the increasing trend of the Rupiah seems to have reached its peak at around Rp 8,500/US\$ in late June (see Figure 2), when IBRA decided to have massive bad-debt fire sales in July and August. The controversial bankruptcy of Manulife Insurance and political uncertainties surrounding the annual session of the MPR had temporarily driven the Rupiah down to more than Rp 9,000/US\$

in late July. However, a successful MPR session put the Rupiah back to around Rp 8,700 - Rp 8,900, and the Rupiah has been stable in that level since then.

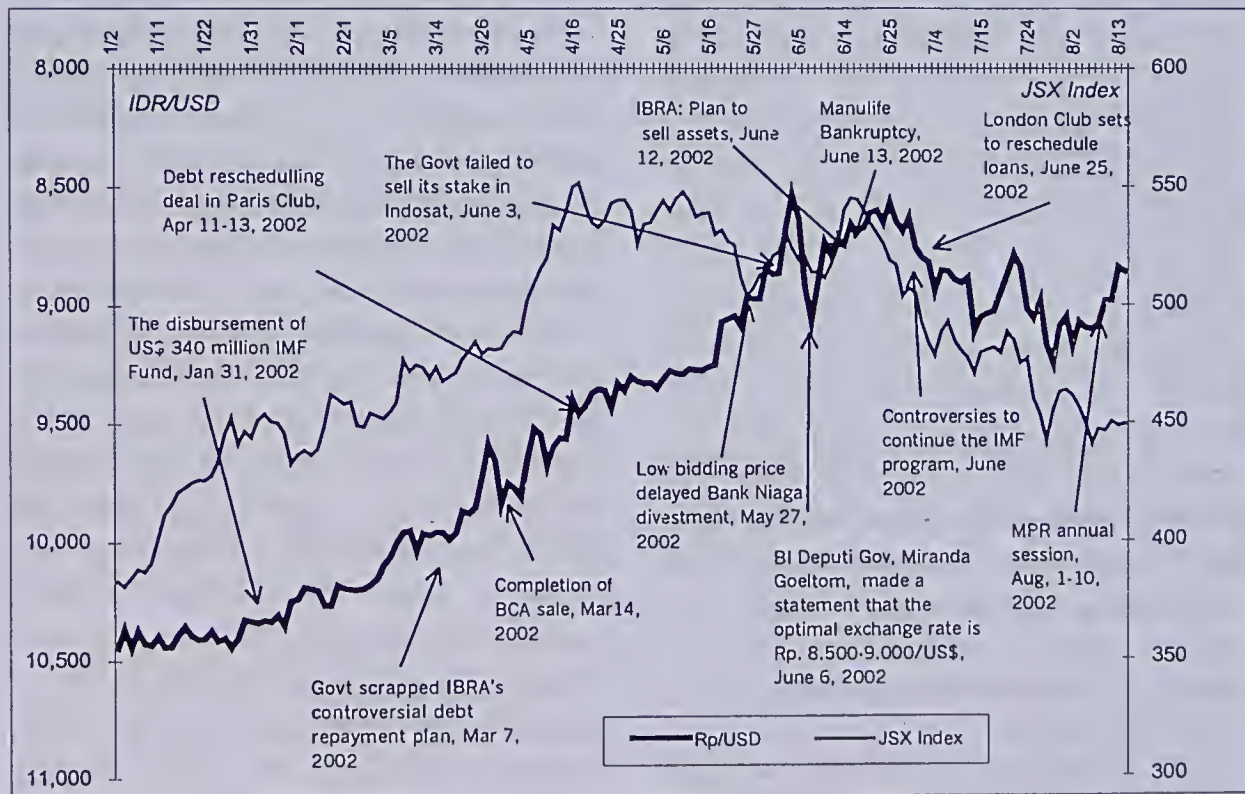
We are expecting a stable Rupiah at this level in the coming months, even though declining interest rates might lead to weaker Rupiah, as people start to convert their Rupiah deposits to US\$. On the other hand, lower interest rate has made the government and corporate bonds more attractive, and any increase in foreign demand of domestic bond will potentially lead to Rupiah appre-

ciation. Lower interest rate opens the possibility of more corporate bond issuance, which in turn attracts more capital inflow and currency appreciation.

After reaching its peak at around 550 in mid June, the JSX index has declined to around 450 in mid August. The controversial case of Manulife bankruptcy was a wake-up call for investors who suddenly realized that the legal system in Indonesia is still weak and unpredictable. Declining stock prices worldwide also led to a bearish market in Jakarta.

Figure 2

THE MOVEMENT OF THE RUPIAH AND THE JSX



Source: <http://www.pacific.commerce.ubc.ca/xr> and <http://www.jsx.co.id>

FISCAL ISSUES

The 2003 Draft Budget: Where Is the Stimulus?

The government budget in 2002 seems to have been on the right track. The targeted budget deficit of 2.5% will likely be met, even though privatization and asset sales have been disappointing in the first half of the year. The exchange rate and growth assumptions look more attainable, due to stronger Rupiah in the past few months. The targeted tax revenue would most likely be achieved, due to the government's aggressive efforts in conducting tax intensification and extensification programs. Tax revenue in the first semester of 2002 accounts for 43% of the target. Meanwhile, from the expenditure side, the reduction in fuel and electricity subsidies has ran smoothly. Foreign financing of the budget deficit has been secured with the successful Paris Club negotiation.

People are now focusing on the 2003 draft budget presented by the president to the parliament on 16 August 2002 (see Table 3). The overall macroeconomic assumptions in the draft budget look ambitious: economic growth will increase from the forecast of 4% in 2002 to 5% in 2003; the inflation rate will drop from around 9% to 8%; official interest rates will decline from around 14% to 13%; and the exchange rate will be Rp. 8,700/US\$ — an appreciation from Rp 9000/US\$ forecasted for this year. Budget deficit is targetted at 1.3% of GDP. While the economic growth of 5% looks too

optimistic, other macroeconomic assumptions are not impossible to achieve. The assumption of 5% real interest rate (13% nominal rate minus 8% inflation) seems too large, and reflects a government's prediction that high-risk premium will remain. Setting 4-4.5% economic growth and 9-10% inflation will make the draft budget more realistic.

From the revenue side, the government plans to raise tax revenue by about 19% from the targeted revenue in 2002. Non-oil and gas tax revenue is targeted to contribute around 72% to the total revenue, a sharp increase from 63% this year. To achieve the target, tax collection, especially income tax applied to companies and individuals will be intensified. The increase in income tax will no doubt lead to lower consumer's demand and producer's earning. To reduce the adverse impact of the policy to raise taxes, any form of tax leakage has to be minimized, and the quality of governance of the tax office has to be improved.

From the expenditure side, the draft budget sends a clear signal that the government cannot be expected to be the engine of growth. Total routine expenditure is likely to decline by about 13% in real terms, from the budget in 2002, especially because the government plans to reduce various subsidies. Nevertheless, balancing funds transferred to the regions for the purpose of narrowing the income gap between central and local governments, will play a role in stimulating growth, as they account for

Table 3

THE SUMMARY OF 2002 AND 2003 DRAFT BUDGET

	2002		2003		
	Budget	% to GDP	Proposed Budget (Rp billion)	% to GDP	Changes 2002-03 (%)
Total Revenues (all domestics)	301,874.3	17.9	327,834.2	16.8	8.6
Tax Revenues	219,627.5	13.0	260,785.4	13.3	18.7
Non Tax Revenues	82,246.8	4.9	67,048.8	3.4	-18.5
Expenditures	344,008.8	20.4	354,097.5	18.1	2.9
Central Government expenditure	246,040.0	14.6	240,881.2	12.3	-2.1
Current Expenditures	193,740.9	11.5	186,381.4	9.5	-3.8
Development Expenditures	52,299.1	3.1	54,499.8	2.8	4.2
Transfer to Regions	97,968.8	5.8	113,216.3	5.8	15.6
Deficit and Net Financing	42,134.5	2.5	26,263.3	1.3	-37.7
Domestic Financing	23,500.8	1.4	16,851.6	0.9	-28.3
Foreign Financing	18,633.7	1.1	9,411.7	0.5	-49.5

Source: Ministry of Finance.

about 30% of total government expenditure. They are expected to provide basis for stronger local consumption.

To finance the deficit of Rp 26.3 trillion or 1.3% of the GDP, the government plans to obtain domestic financing of Rp 16.9 trillion, by raising revenues from privatization, selling assets, issuing bonds and using excess funds carried over from 2002. We are concerned that the government might face some difficulties in meeting the asset selling target because the recent asset sales has left little valuable assets left at IBRA. This means the government needs to be more aggressive in conducting privatization program.

With a deficit of less than 1.3% of the GDP and the monetary effect-estimated by calculating the difference between domestic government spending

and tax generated from domestic economy of only Rp 92 trillion, compared with Rp 121 trillion this year, apparently this draft represents a very tight budget. Therefore, we are encouraged by the efforts of the government to press forward the reform agenda and to keep the fiscal deficit on track.

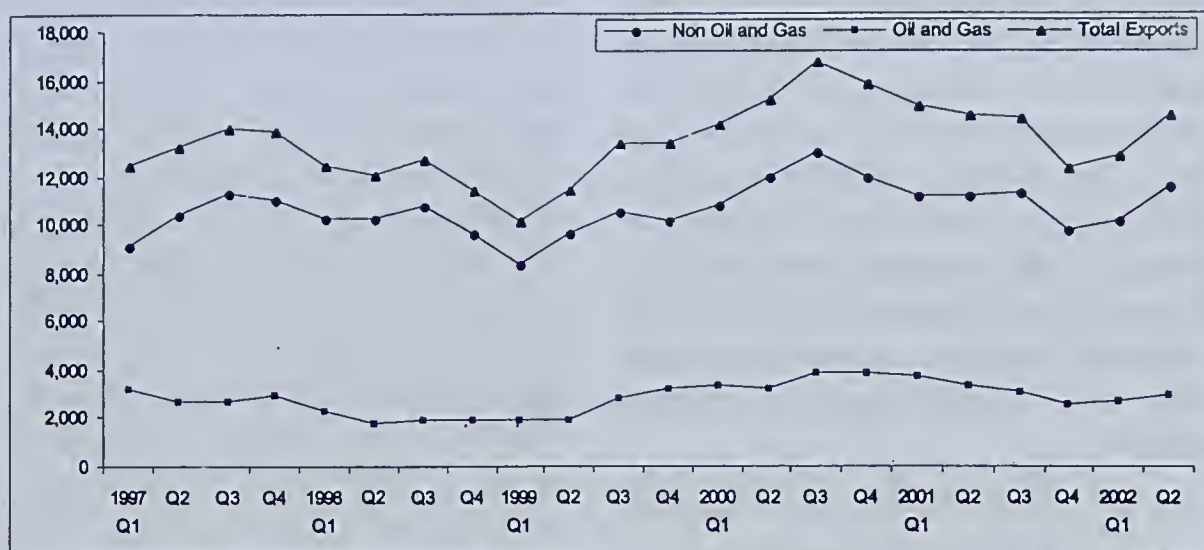
BALANCE OF PAYMENT

Export and Imports: Some Encouraging Signs

Although the export figure for the first half of this year (US\$27.4 billion) was still lower than that of the same period last year (US\$29.4 billion), there has been a steady improvement in Indonesia's exports since the '9-11' tragedy (see Figure 3). We owe this to the strong performance of manufacturing commo-

Figure 3

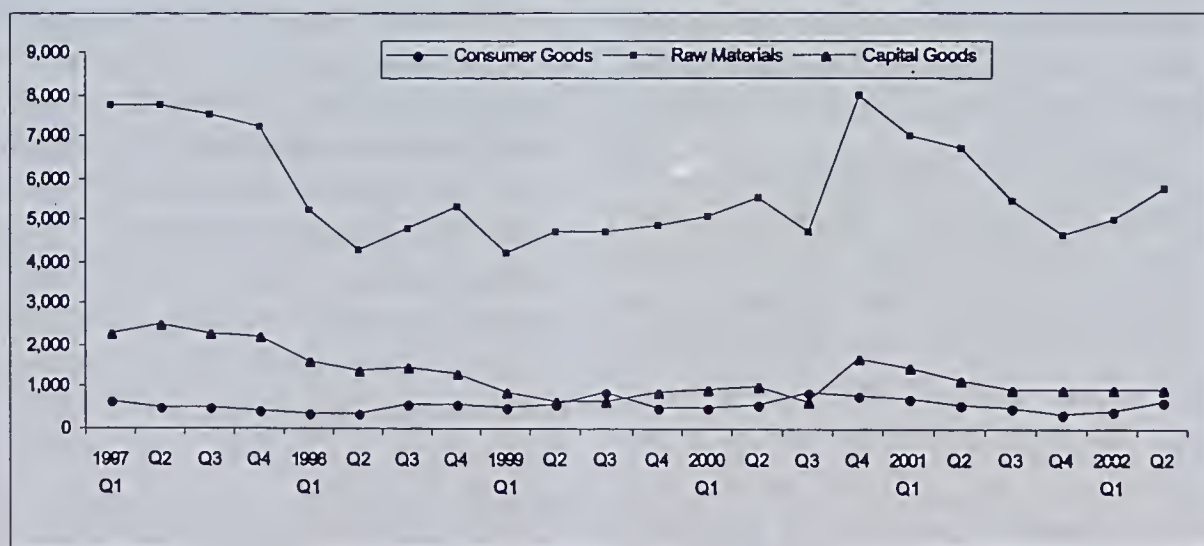
THE VALUE OF QUARTERLY EXPORTS (US\$ MILLION)



Source: Economic Indicators, Statistics Indonesia.

Figure 4

THE VALUE OF IMPORTS BY CATEGORY (US\$ MILLION)



Source: Central Board of Statistics.

dities, which increased by 5% from the second semester of 2001. In contrast, oil and gas exports declined slightly by 1% from the second semester of 2002. Mining also declined by 4%.

There have been some structural changes in the pattern of exports. While footwear, textile and garments used to top the list of major exports, other manufactured products, such as appliances/

home-lighting, machinery/ mechanical equipments, machinery/electrical equipments and man-made style of fiber topped the export in the first semester of 2002, which increased by 9.6% compared to that in the last semester of 2001. The footwear association reported that foreign buyers have begun to switch to other countries, such as China, Vietnam and Thailand. Similarly, the textile and garments industry association also reported a sharp decrease in foreign demand.

It is a great challenge for Indonesia to sustain the growth of export for the rest of 2002. The external condition is currently not favorable because the demand for export remains weak due to the global downturn. While from the domestic side, institutional reform in customs and other trade-related government institutions, is yet to be realized.

Imports have also performed better following the '9-11' tragedy. Import figures in the first half of increased by 6.5% compared to the second half of 2001 (see Figure 4). The official figures of imports are certainly much lower than the actual imported goods if we take into account illegal imports. Despite the heavy complaints of smuggling, there has been no effective action undertaken yet to curb those illegal activities.

Capital Accounts and Investment: Gloomy Picture

For the first time since the crisis unfolded, net private capital outflows in

the fourth quarter of 2001 dropped to US\$0.18 billion, significantly lower than the average of US\$2.5 billion in each quarter observed during the previous four years. However, the preliminary BOP data in the first quarter of 2002 indicates otherwise, showing a sharp increase of US\$1 billion, mainly due to a large FDI outflow of US\$2.2 billion and a net portfolio outflow of US\$0.4 billion. It is important to note, however, that there has been a steady increase in 'other' private inflows since the last quarter of 2001. This is partly due to the return of some 'Indonesian' money parked overseas as a result of improved security and more stable political situation after the presidential succession in August 2001.

Investment during the second quarter of this year appears gloomy as the overall approved investment reported by the Board of Investment, declined by 42% for foreign investment and by 72% for domestic investment. Some existing foreign investors such as *Matshushita Electrics* indicated that they might relocate their investment from Indonesia (*Kompas*, August 26, 2002). In addition, around 170 textiles and garment producers were reported to have stopped their production activities while some others have cut their production. PT. Unilever Tbk and China National Offshore Oil Corporation (CNOOC), who recently bought Repsol-YPF, are among the very few foreign companies who have indicated on expanding their investment activities.

The Bank Indonesia confidence survey also shows a gloomy long-term investment outlook, which is indicated by increasing long-term risk premium. This would explain why big investments are unlikely to take place in the near future and, unless there are serious efforts to resolve issues, such as security, institutional problems and legal certainty, the long-term risk premium is not likely to fall soon. Moreover, the government and the House of Representatives are still unable to agree on the investment bill, a necessary legal basis for investors in doing business in Indonesia.

BANKING AND FINANCIAL ISSUES

The Phasing Out of Blanket Guarantee

The government has announced its plan to phase out blanket guarantee on bank deposits—the scheme introduced in early 1998 in response to bank runs—but without specifying any definite date for its implementation. Under the law, the government should announce the termination of the scheme six months before its implementation (see Table 4). Initially, the starting date for the phasing out of the guarantee was set for early next year. However, that has been delayed, partly on Bank Indonesia's reservation. BI argues that certain institutions or institutional arrangements, such as limited liability deposit insurance, should be in place before the removal of the guarantee.

On the other hand, there are those who argue that the government should

have terminated its guarantee on inter-bank loans to discipline banks and reduce moral hazard. In fact, we also believe that the gradual phasing out of blanket guarantee would develop some kind of competition and natural selection mechanism in the banking system where the depositors are expected to place their deposits at more credible banks. Government blanket guarantee should not be used to support and prevent bad banks from collapse.

Reprofiling of Government Bonds

The government will soon begin to restructure or reprofile the government bonds that are now held by various banks, starting with bonds matured in 2004. The main idea is to replace shorter-term recapitalization (recap) bonds with longer-term ones through exchange offer. By reprofiling the maturity of the bond, the government could smooth-out the maturity of the bonds, extend it over longer periods of time, and avoid a massive debt burden in the near future. The decision, however, has to be approved by the Parliament.

A large fraction of the government bonds will mature between 2004 and 2009 and this needs to be properly managed so as to avoid creating undue problem to the government fiscal balance, also known as "fiscal time bomb". For instance, for the current year, the interest payment alone is about Rp 88.5 trillion or about 27% of the government's domestic revenue. For the next

Table 4

**SCHEDULE FOR THE PHASING OUT
AND TYPES OF GOVERNMENT'S GUARANTEE**

First Stage: 6 month after the announcement

On balance sheet:

- Cash collateral
- Import facilities
- Securities, e.g., floating rate notes (FRN), floating rate certificate on deposits (FRCD), medium term notes (MTN), Bonds
- Direct loans

Off balance sheet:

- Import transaction e.g., L/C, standby L/C, etc.
- Bank guarantee
- Currency swap
- Local L/C

Second Stage: 12 months after the announcement

- Inter-bank loans
- Third party funds, e.g., deposits, CD, and on call deposit above Rp 5 billion

Third Stage: 18 months after the announcement

- Third party funds
 - Establishing limited liability deposit insurance up to Rp 100 billion
-

year, the total interest payment is expected to be lower, about Rp 80.9 trillion, of which-about Rp 55.1 trillion-will be on domestic debt. Without reprofiling the maturity of the bond, the principal payment of the bond alone would be more than Rp 52 trillion in 2004 and more than Rp 60 trillion in 2005 resulting in an unbearable domestic debt burden.

By reprofiling the bonds, the risk of fiscal time bomb in 2004 and beyond would be significantly reduced. However, the cost of managing the bonds would increase because the government is delaying the payment of the principal, thereby paying the interest for a longer period of time.

IBRA's Asset Sale

The Indonesian Bank Restructuring Agency (IBRA) has completed the massive sales of its bad loans with a total face value of more than Rp 135 trillion. With this sale, IBRA is expected to meet its target to raise Rp 42 trillion this year, which is partly used to finance the government budget deficit.

The sale of asset by IBRA, however, has never been free from controversy. *First*, the recovery rate of these assets is very low, only about 28.3% of the total asset sold, and about 17.1% of the total asset offered for sale. *Second*, the sale could not reduce the amount of outstanding government bond. One objective of the recent credit asset sales

by IBRA was to encourage recapitalized ailing banks to participate in the bidding of the assets offered and swap those assets with recap bonds, which in turn would reduce the amount of recap bonds in circulation. From this perspective, some have regarded the sale as a failure because the payment in the form of bond is only about Rp 4.5 trillion while the remainder of Rp 18.6 trillion is in cash. *Third*, there is more allegation of irregularities and corruption in the sale process. The House of Representatives has mentioned that it would call the agency for a special hearing, with the possibility that the House would ask the Supreme Audit Agency (BPK) to investigate the sale process.

OTHER ISSUES

Saying Good-Bye to the IMF?

The IMF, after having finalized the review of the sixth Letter of Intent (LoI) earlier in August, sets to disburse another US\$360 million of loan tranche to Indonesia, subject to the agreement of the Board of Executives in Washington D.C. In general, the IMF expressed its satisfaction with the government's performance in implementing economic reform policies. But the Fund also warned that the government should focus on restructuring the country's banking sector and re-establishing investors' confidence to achieve a sustainable macroeconomic stability.

Meanwhile, in the past few months, there have been intense debates over

the role of the IMF in Indonesia. After four years, IMF's prescription does not seem to be effective in bringing the country out of the crisis. The program is supposed to end in November this year, but the government has already extended the program for another year to November 2003, as part of conditions set by the Paris Club. This caused disagreement between cabinet members, particularly between the State Minister of National Development Planning Kwik Kian Gie, who argued that the government should not continue the IMF program, and Chief Economic Minister Dorodjatun Kuntjoro-Jakti and also Finance Minister Boediono who supported the extension.

It is worth noting that the US\$347 million loan disbursement did not appear to affect the market sentiments much. Indeed, the exchange rate and stock market index was strengthening, but it has been so for weeks before the disbursement. In other words, the news about IMF may no longer be significant to improve market sentiments. Realistically, the government does not have any right arguments to end the relationship with the IMF. Doing so might leave the country with relatively no capital inflows, which will mean slower economic recovery. However, it is not to say that the government should be tied up with the IMF for a prolonged time. Instead, the government should conduct the reform program seriously, and at the same time, the government should prepare the correct strategy to settle the debt.

The New Labor Bill Controversy

Labor and employers are on a virtual agreement in rejecting the Labor Bill package being discussed in the House of Representatives, both for different reasons. Employers, represented by the Indonesian Employers Association (Apindo), argue that the bill will hurt businesses and decrease the competitiveness of the country's labor market. The clauses specify that employers must continue to pay the full salaries for striking workers, as well as half of the salaries for workers unable to work due to criminal trial. Apindo claims this contradicts the universally adopted 'no work no pay' principal. Apindo also appeals against clauses that require employers to provide severance pay to workers who voluntarily resign.

Workers, on the other hand, consider the bill very much biased against them. The Indonesian Committee of Workers' Union (KSPI), one of the many labor representatives, raised five points for the basis of rejection. *First*, the bill makes it difficult for workers to strike. *Second*, the procedure for employers to terminate workers is considered too simple. *Third*, the clauses on severance payment and appreciation are somehow unfair. *Fourth*, employers are still allowed to pay only 80% of the minimum wage standard for workers in probation. *Fifth*, rulings do not specify the types of jobs that are eligible for contract-based works.

In 1997, the government and the parliament issued the Law No. 25/1997 on Manpower. The government then is-

sued a decree to delay the implementation of the law until October 2002, as it was very controversial. Theoretically, if no new law were ratified until the deadline, the controversial Labor Law No. 25/1997 would be automatically reinstated. But such scenario is unlikely, since a chapter of the controversial law had been ratified as the Law No. 21/2000 on Labor Unions. In order to avoid more controversies in the future, the government had better delay the ratification of the bill, while making some revisions and improvements.

Legal Uncertainties: Foreign Investors Are in the Middle of No-Where

As stated before, the existing legal systems is dubbed to have created a repulsive climate for foreign investors. To illustrate this, two unpopular cases that received a great amount of attention are presented here. The *first* one is known as the Manulife case. Last July, the Supreme Court overturned a controversial bankruptcy ruling against PT Asuransi Jiwa Manulife Indonesia (AJMI), a local unit of the Canadian-based Manulife Financial Corp. The bankruptcy ruling was made after a recipient of the now defunct, PT Dharmala Sakti Sejahtera (DSS), the one-time local partner of Manulife, filed a bankruptcy petition in May on the grounds that AJMI had refused to pay Rp 22.4 billion in dividends in 1999 to DSS. Eventually, the government decided to investigate and dismiss three judges who were allegedly bribed when handling the case. The decision to overturn the bankruptcy ruling was widely welcomed by foreign and

local investors who had been complaining about unpredictable judgment on commercial matters by Indonesian courts.

The second case occurred in early July 2002, when the East Kalimantan government dropped a lawsuit against British Petroleum (BP) PLC and Anglo-Australian mining company Rio Tinto PLC. The suit, which was filed earlier this year, sought to force the two companies to sell a 51% stake in their coal-mining joint venture, PT Kaltim Prima Coal (KPC)

to the East Kalimantan government. Indeed, the foreign companies are obligated by their contract with the central government to offer the shares to Indonesian investors but it did not specify who would have the right to buy the stake. The central government had threatened legal action against the local government unless the lawsuit is dropped. Although the lawsuit was finally dropped, the disputes had illustrated the problems of doing business in Indonesia's outlying regions in the wake of Indonesia's decentralization drive.



PEACE BUILDING AND STATE BUILDING IN EAST TIMOR

Edited by Hadi Soesastro & Landry Haryo Subianto

Published by: CSIS, Jakarta

This volume contains six papers originally prepared for a Task Force created by the Council for Asia Europe Cooperation (CAEC). The study of East Timor, which was undertaken as a collaboration between scholars from East Timor, Australia, and Indonesia, aims mainly to examine East Timor's challenges and how it can best respond to them.

The first paper written by Dionisio Babo-Soares examines the political transition in East Timor. He identifies four types of players that shape the political transformation in East Timor: UNTAET, the East Timorese political community, the ordinary people, and the Catholic church. The second paper by James J. Fox presents an assessment of UNTAET's role in building local capacities for the future. The third paper, which was written by Dionisio Babo-Soares, discusses law and order, including the management of internal security in East Timor. The fourth paper, presented by Rizal Sukma, analyzes East Timor's security challenges. This is followed by a paper written by Helder da Costa and Hadi Soesastro. They present their views and assessment on the economic development in East Timor and its future challenges. The last paper by Landry H. Subianto discusses the role of various international institutions in the process of peace-building and state-building in East Timor.

This volume is recommended for those who are interested in the studies of East Asia and Southwest Pacific, in particular of East Timor.

2002. 1st Ed., vi + 170 pp.; 25 cm, ISBN 979-8026-77-2, Rp 40.000,00/

Indonesia's New Constitution: A Peaceful Reform

Staff, Department of Politics and Social Change, CSIS

INDONESIA has just moved forward to another significant step of its reform process with the completion of the amendment of the 1945 Constitution by the People's Consultative Assembly (MPR) in the early hours of Sunday, 11 August 2002. Two previous significant steps were the toppling down of President Soeharto in 1998, and the relatively democratic 1999 General Elections. The completion of the amendment proves that Indonesia is indeed capable of managing a peaceful process of reform.

The major result of the session is the amendment of the Indonesian 1945 Constitution. This result also concluded the amendment process of the 1945 Constitution that had started since the MPR General Session in 1999. In addition to the substantive achievement in the new constitution, the process of amending it should also be applauded as it proved

the level of political maturity of the elites in dealing with the crucial political and ideological issues without going through harsh political violence.

PEACEFUL PROCESS

In that very sense of the process, at least two achievements need to have special notes. The *first* is the rejected calls for imposition of Islamic Syariah law, which was related to the amendment to Article 29 of the 1945 Constitution, stating that "The State shall be based upon the belief in the One and Only God." This issue had become hot debates during the Assembly's session. A number of political parties wanted to maintain the original article; while a number of Islamic parties proposed the amendment of this article by supplementing it with words contained in the Jakarta Charter, that is "The State

shall be based upon the belief in the One and Only God with the obligation to implement the Syariah Law for its devotees". This proposal enjoyed the support of Islamic organizations rallying outside the MPR building, for example Hizbu Thahrir, the Islam Defenders Front (FPI) and Hizbollah. Another political factions in the Assembly proposed to amend it with a new alternative stipulating: "The State shall be based upon the belief in the One and Only God with the obligation to implement religious teachings for all devotees of religions."

Interestingly, this issue could be discussed and debated openly — something that could never happen before. Besides, the discussion on the pros and cons to the calls for imposition of the Syariah Law had no longer dealt with Moslems vs non-Moslems, but it involved the Moslems themselves. Finally, the decision to maintain the original article was taken not through voting but consensus mechanism. After all, the supporters of the Syariah Law realized consciously that their proposal would not have considerable support to be implemented. This has also confirmed the acknowledgement of religious plurality in Indonesia.

The *second* was the withdrawal of the military and the police from politics. This is indeed another thing to be appreciated. Many people suspect that the TNI withdrawal was an astute and calculated move. Originally, the TNI was to withdraw in 2009 but now it is changed to 2004. With the withdrawal of the military from politics, it is now

the chance for civilian politicians to prove they can manage the country well and serve for the prosperity of Indonesian people.

THE SUBSTANCE

The constitutional amendments enacted by the MPR since 1999 are not perfect by any measure. For many people, they are still far from the ideal that would put Indonesia on a path toward a prosperous modern state under democratic civilian rule. But the present basic law is certainly much better than the original 1945 Constitution in ensuring that power-greedy dictators will no longer rule the nation. At the very least, the amended 1945 Constitution has stripped away some of the powers of the president and of the MPR, and restored them to their rightful owners: the people.

At least nine new principles of system of governing Indonesia are adopted in the new Constitution of Indonesia. These are as follows:

1. Unitary State with federal arrangements;
2. People's sovereignty;
3. (Religious) plurality;
4. Statehood based on law;
5. Separation of Powers between Legislature, Executive and Judiciary;
6. Mechanism of checks and balances between State Institutions;
7. Independent Judiciary;
8. Social Market Economy; and,
9. Respect to Human Rights.

In political terms, the new principles have implicated accordingly to the substantial change in the structure of the Indonesian state as well as in major recruitment procedures of public offices. The first refers to the change from an integralistic state with an all-powerful highest institution of state (the People's Consultative Assembly or MPR) to a state with constitutional checks and balances and with separation of powers between the legislature, executive and judiciary. The latter refers to the adoption of the mechanism of direct presidential election and the new procedures of general election for members of the representative institutions, i.e. the House of People Representatives (DPR) and the House of Regional Representatives (DPD).

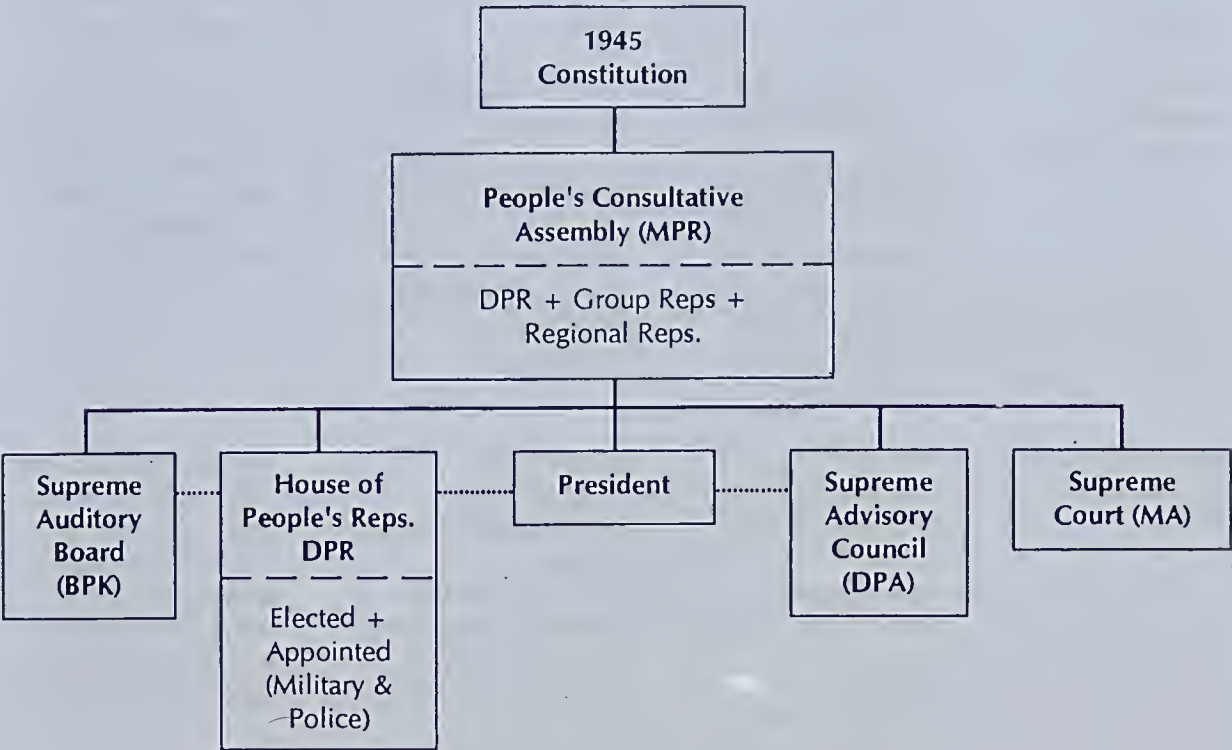
There is also a new arrangement for the judiciary power. Two judicial institutions with different functions are formed to exercise the power. These are the Supreme Court and the (new) Constitutional Court. The first exercises the judiciary power to organize the judicature in order to enforce law and justice, to hear a trial at the highest (cassation) level, and to review ordinances and regulations made under any law against such law. The latter has the right of judiciary power to try a case at the first and final level, to have the final power of decision in reviewing laws against the Constitution, to determine disputes over the authorities of state institutions, to decide over the dissolution of a political party and the disputes on the result of general elections, and to issue a decision over an opinion of the DPR concerning alleged violations by the Pres-

ident and or Vice President of the Constitution.

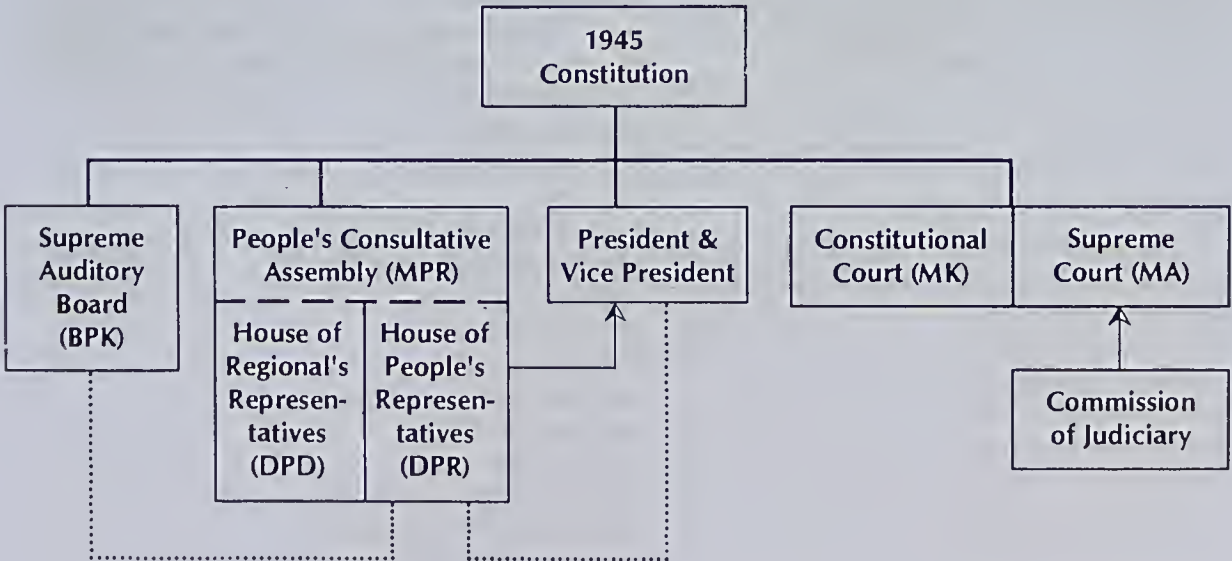
In more detail, the major changes made to the 1945 Constitution by the four amendments are:

- The sovereignty of the people is no longer exercised in full through the MPR but is implemented in accordance with the Constitution itself.
- The MPR has limited specific functions only. These are to consider constitutional amendments, to swear in the elected President and Vice-President, to fill casual vacancies for Vice-President and double casual vacancies for President and Vice-President, and to decide on the action to follow a ruling by the Constitutional Court that an impeachment charge is well grounded.
- The MPR is to be made up entirely according to the principle that representatives should be elected. It will consist of the members of the DPR and the members of the new regional chamber, the DPD.
- The DPR and the DPD are institutions representing respectively the people and regions.
- The DPR has legislative powers; while the DPD supports the implementing roles of DPR on certain issues relating to regional autonomy, centre/region relations and natural resource management, and oversight powers on these issues plus budget management of tax, education and religion.
- The president and vice-president will be elected as one ticket in a direct

STATE INSTITUTIONS OF INDONESIA
PRE-AMANDMENT TO THE 1945 CONSTITUTION



STATE INSTITUTIONS OF INDONESIA
POST-AMANDMENT TO THE 1945 CONSTITUTION



————— : command lines; : coordination lines; —————➤ : oversight line

Table 1

THE ROLE OF STATE INSTITUTIONS

Institution	Old System	New System	Notes/Discussion
People's Consultative Assembly (MPR)	<ol style="list-style-type: none"> 1. Exercise fully the sovereignty of the people 2. Amend and Determine Constitution 3. Determine Guidelines of State Policy 4. Elect and Dismiss the President and Vice President 	<ol style="list-style-type: none"> 1. Amend and Determine Constitution 2. Inaugurate elected President and Vice President 3. Dismiss the President and Vice President according to the Constitution 	The new system has fundamentally changed the status of the MPR from an omnipotent to a limited-potent state institution.
House of People Representatives (DPR)	<ol style="list-style-type: none"> 1. Approve bills 2. Oversee the implementation of state policy 3. Approve annual state budget 	<ol style="list-style-type: none"> 1. Establish laws 2. Hold legislative, budgeting and oversight functions 3. Recommend to the President in appointing ambassadors, and in receiving ambassadors of other nations 4. Recommend to the President in granting amnesty and the dropping of charges 	The new roles of DPR may implicate to the domination of this institution over other state institutions, and thereby thwart the function of checks and balances mechanism.
House of Regional Representatives (DPD)	No such House, but a political fraction in the MPR with no daily effective roles	<ol style="list-style-type: none"> 1. Propose bills to the DPR related to issues on regional autonomy, relations of central and local government, management of resources and fiscal balance 2. Participate in the discussion of bills related to issues of regional autonomy, relations of central and local government, management of resources and fiscal balance 3. Provide considerations to the DPR on the state budget and bills related to taxation, education, or religion 4. Oversee the implementation of regional autonomy policy, and submit the results of such oversight to the DPR 	Whit such roles, DPD has no effective power of representing the interest of regions of the Indonesian state.

Institution	Old System	New System	Notes/Discussion
Supreme Court (MA)	<ol style="list-style-type: none"> 1. Exercise the authority to hear a trial at the highest (cassation) level 2. Review ordinances and regulations made under any law against such law 	<ol style="list-style-type: none"> 1. Have the power to organize the judiciary in order to enforce law and justice 2. Exercise the authority to hear a trial at the highest (cassation) level 3. Review ordinances and regulations made under any law against such law 	
Constitutional Court (MK)	No such court	<ol style="list-style-type: none"> 1. Has the authority to try a case at the first and final level and have the final power of decision in reviewing laws against the Constitution 2. Determine disputes over the authorities of state institutions 3. Decide over the dissolution of a political party 4. Decide over the disputes on the result of general elections 5. Issue a decision over an opinion of the DPR concerning alleged violations by the President or Vice President of the Constitution 	This court should be established at the latest by August 17, 2003
Commission of Judiciary	No such commission	<ol style="list-style-type: none"> 1. Propose candidates for appointment as justices of the Supreme Court 2. Maintain and ensure the honor, dignity and behavior of judges 	
Commission of Constitution	No such commission	Synchronize and harmonize chapters, clauses and articles of the amended 1945 Constitution.	The membership, structure and authority of the Commission of Constitution will be arranged by the Ad Hoc Committee of the MPR, and shall be decided and enacted by the Annual Session of the MPR in 2003

- election, with two rounds if no candidate achieves 50% + 1 of the vote and at least 20% in half the provinces in the first round.
- The impeachment process relating to the president and vice president excludes removal from office on policy grounds and under which the legal decision on whether grounds for impeachment exist is determined by the new Constitutional Court.
 - Establishment of a Constitutional Court separated from the Supreme Court.
 - Establishment of an independent Judicial Commission dealing with proposals for Supreme Court appointments and with judicial ethics issues.
 - Abolition of the Supreme Advisory Council (DPA) and the institution of a presidential advisory council as part of the executive branch.
 - Constitutional backing for the principles of regional autonomy.

- Human rights provisions added in line with the larger part of the Universal Declaration of Human Rights.

A comparison between the old and new structure and functions of the Indonesian state institutions can be seen in the following charts and Table 1 respectively.

COMPOSITION OF REPRESENTATIVE INSTITUTIONS

The number of members of both DPR and DPD remains uncertain. However, this will be determined through and in the Law on Composition and Structure of DPR, DPD and the MPR. Although the law has not yet been made, a bill on this issue is being deliberated in the DPR. The DPR is expected to legislate the bill in December 2002 at the latest.

Based on the bill, the membership of the DPR is designed to have 550 members. No clue how this number

Table 2

MEMBERSHIP AND RECRUITMENT OF REPRESENTATIVE INSTITUTIONS

Institution	Membership	Recruitment	Notes
DPR	550	Elected, party based, proportional representation with province as electoral district	Represent people
DPD	No more than 1/3 of the 550 DPR	Elected, individual based, district system with province as electoral district	Represent regions
MPR	DPR + DPD	All elected	Represent both people and region

came up. But, according to the constitution, the total number of DPD members will be no more than 1/3 of the total number of the DPR members. As stipulated in one clause of the bill, each province should elect four representatives. Indonesia now has 31 provinces, which will make up the total number of the DPD members to 124 (no more than 1/3 of the total number of the DPR members). Therefore, there is a strong demand to add one more representative for each province.

THE NEW PROCESS OF DIRECT PRESIDENTIAL ELECTION

The amendment of the 1945 Constitution introduces a new process of presidential election in Indonesia. The process adopts a direct presidential election in which the President and Vice-President are to be elected as a single ticket directly by the people.

The basic procedure of this presidential election as stipulated by the new Constitution goes as follows:

1. Each ticket of candidates for President and Vice-President shall be proposed prior to the holding of the general election by political parties or coalition political parties which are participants of the general election;
2. Any ticket of candidates for President and Vice-President which polls a vote of more than fifty percent of the total number of votes during the general election and in addition polls at least twenty percent of the votes

in more than half of the total number of provinces in Indonesia shall be declared elected as the President and Vice-President; and,

3. In case there is no elected ticket of candidates for President and Vice President, two tickets of candidates that get the first and second most votes in the general election are directly elected by the people and the ticket that gets the most vote is elected President and Vice President.

A more detail procedure of this new direct presidential election will be further composed in the law that shall be established by the DPR. If the next presidential election is scheduled for 2004, the law should be completed by the DPR by the end of this year.

Once again, Indonesia will have another new political experience of direct presidential election. There is some sceptism that this new experience will only endanger the social integration of Indonesian society. However, there is great optimism that Indonesia will succeed to have it, as the grass roots have been familiar with direct election for their local leaders. In all, the adoption of direct presidential election should have satisfied one achievement of political reform in Indonesia.

Although it is still far to ensure the most potential candidates for the 2004 direct presidential election, there are several prominent leaders that should be eligible to be nominated and or have

intention to nominate as candidates of President and Vice President. This is reflected by a recent national polling, resulting more or less the current level of popularity of the following pairs of leaders: Megawati Soekarnopoetri — Susilo Bambang Yudhoyono (15,5%); Amien Rais — Yusril Ihza Mahendra (11,5%); Amien Rais — Megawati (10,6%); Megawati — Hamzah Haz (8,0%); and Amien Rais — Yudhoyono (5,4%).¹

According to some analysts, Indonesia needs a "spiritual leader" to lead this transiklional process to democracy. Unfortunately, such a leader could hardly be found among the current stock of leaders who mostly come from political parties. But, to name a few, the needed spiritual leaders could be Ahmad Syafii Maarif (Muhammadiyah), Nurcholish Madjid (intellectual), Salahuddin Wahid (Nadlatul Ulama), and Azyumardi Azra (intellectual).²

WEAKNESSES OF THE NEW CONSTITUTION

Some of the weaknesses of the new amended Constitution can be listed as follows. *First*, the amendments still have problems regarding checks and balances mechanism. The current system of amendment is 'heavily legislative'; and the new bicameral system is half-hearted because the regional legislative

councils do not share the role of decision-making with the national legislature.

Still part of the checks and balances problems is the relationship between the President and the House of Representatives (DPR). Now the role of DPR is much stronger than the President. This is understandable because of the history of an authoritarian regime under Soeharto, where the DPR was very weak. But now the House seems too strong, there is no check and balance mechanism between the president and the House. If the President proposes a law, the House has no obligation to pass the law, while if the DPR proposes a law and the President vetoes it, then DPR only needs to wait for 30 days to implement the law. The role of the president is very weak, but the presidency will have very strong legitimacy (after 2004), so there is a gap between this strong legitimacy and the president's power.

Second, the impeachment process in Article 7 of the new Constitution still gives the authority to the MPR to evaluate the decision of the (future) Constitutional Court. So it turns out that the MPR still has such authority. Instead of emphasizing the rule of law we still have a process prone to politicization; the MPR might take a different view from the Constitutional Court.

Third, in Article 28 of the Constitution, there is still the retroactive clause barring investigations into past human rights violations which will save the likes of Golkar people (from prosecution). This

¹See *Kompas*, 31 August 2002.

²See "Calon Presiden Independen", *Kompas* 24 Juli 2002.

is a concrete example of politicking that affects the substance of the constitution.

Fourth, the amended Constitution failed to mention crucial auxiliary state institutions, such as the independent and permanent General Elections Commission (KPU), an anticorruption commission, the National Commission on Human Rights (Komnas HAM) and the National Ombudsman. The inclusion of such state institutions in the Constitution, aside from the fact that their presence was stipulated under legislation, would give a stronger legal basis to their work in providing an appropriate system of checks and balances on the government.

Finally, there is a crucial issue of Clause 37 on the form of the state. Without public knowledge it was suddenly made into a non-amendable article. Regardless of whether the form of the state should be changed, this very crucial clause cannot be made into a non-amendable article.

IMPACTS AND CONSEQUENCES

The full package of changes should take immediate effect. Transitional provisions provide that where new legislation and institutions do not yet exist, the existing arrangements stay in place. For example, the Supreme Court will undertake the functions of the Constitutional Court until this body is set up, which is to happen by August 2003. The existing MPR and DPR will stay in place until the 2004 elections.

A considerable volume of implementing legislation and other legal instruments is now necessary. First, the MPR should review the status of its existing decrees (TAP MPR), because it will no longer have the power to use these instruments to make policy directions. Some of these decrees --for example, the decree establishing the hierarchy of status of legal instruments-- will need to be replaced by appropriate laws.

The MPR will also review its standing orders to bring them into line with the Constitution. This means that the 2003 MPR session will receive and hear a report from the President without discussion, and that there should be no MPR session to receive an accountability report in 2004 before the election.

At the same time, the Government and the DPR need to prepare and debate the laws before being enacted. So many clauses in the constitution cite further regulation through laws, which leaves too much power in the hands of legislators. There are at least 30 new legislations required by the constitution. Among the 30 new laws to be made, some are urgently required in the perspective of two years to come. These are as follows:

- The new electoral and political party legislation.
- Legislation for direct presidential elections.
- Legislation on the structure and composition of representative institutions, in particular the new provisions for the DPD.

- Legislation on the establishment of the Constitutional Court.

Another problem is the urgency of a constitutional commission. Its formation will still depend on the MPR. As contained in the MPR decree on the establishment of the commission, the MPR's Working Body will determine whether such a commission will be established by 2003. The fact that the commission is ruled by an MPR decree has made it very weak. The next Annual Session could make it void.

It can be expected that within the next two years, Indonesia is likely to debate again on some other crucial political issues. During that period, political conditions might go ups and downs. But, with the experience of succeeding the completion of the amendment to the constitution, there is a lot of assurances that the coming political process of completing the political laws might also run successfully and peacefully. What can be learnt from it is that this coming political process should involve more public participation as to ensure the transparency of the process

and the sense of belonging of the public to the results of the political process.

That also emphasizes the fact that although a relatively democratic basic law has already been established in Indonesia, it would be meaningless without fundamental cultural changes of the Indonesian people. The basic law creates the legal justification for the setting up of a democratic political system. It is only the Indonesian people's commitment and consistency to implement the values and principles of democracy that can guarantee the democratic political system to function.

The next two year period (2002-2004) will be the first significant test for the Indonesians whether or not they are capable of sustaining further process of peaceful democratic reform. Nobody said the road to democracy would be short and painless. When this nation opted for reform rather than revolution, it might take longer but the road to democracy and prosperity could be more certain. Today, with the MPR having completed the constitutional amendment process, the Indonesian people are probably only halfway there.

Indonesia and the September 11 Attacks: Domestic Reactions and Implications*

Rizal Sukma

INTRODUCTION

AS history has proved, the structure of international order has often changed with the occurrence of a dramatic defining event. The end of the Second World War in 1945, for example, served as a crucial event for the emergence of the Cold War international order. When the Berlin Wall fell in 1989, the international community saw it as the beginning of the birth of Post-Cold War order. Now, the Post-Cold War international order was said to have been brought to an end by the collapse of the World Trade Centre in New York on 11 September 2001. Indeed, the horrific terrorist attacks on the United States (US) were a despicable example of an evil act against humanity. It serves as a wake-up call for anyone that terrorism has taken a new turn both in terms of its methods, forms and the damage it

inflicted on human lives. For the US itself, the barbaric attacks expectedly forced it to respond swiftly through a declaration of global war against terrorism, starting with a military strike against Afghanistan.

The impacts of the September 11 were soon felt, and still are, across the globe. It clearly reinforces the notion of the borderless world. When the impacts of the attacks were immediately felt in national domain of almost every countries, the traditional notion of territorial boundaries-that signifies the separation of independent sovereign states from each other-becomes less relevant. This, for example, is clearly demonstrated in various domestic reactions in many parts of the world, especially within the Muslim world. Indonesia is no exception, and soon faced with a formidable challenge in handling the impacts of the event on its domestic scene. When the US and its allies began to point to Osama bin Laden and his associates in the Al-Qaeda as the perpetrators, the pressure was particularly mounting on Indonesia's government. As the largest Muslim country in the

*Paper presented for the Workshop of APAP Project on "Asia Pacific Regional and Global Order in the Post 9-11 World", Seam Reap, 26-28 February 2002.

world, Indonesia's reactions to the September 11, and the subsequent American-led war on terrorism, would certainly not be lost on the US, and indeed on the international community.

This paper analyzes the Indonesian reactions to the September 11 and its aftermath. The discussion is divided into three sections. The first section examines the Indonesian government's response to the event of September 11 and subsequent American military campaign in Afghanistan. The second section examines the wider debate on the issue within Indonesia's Muslim community and locates the place of both radical and moderate voices within that debate. The third section discusses Indonesia's position in dealing with the issue of terrorism, especially amidst suggestions on the presence of terrorist networks in the country.

THE GOVERNMENT POSITION: STRATEGIC AMBIGUITY OR PLAIN HYPOCRISY?

In general, Indonesians—both within and outside the government, and across different ideological spectrum—were quick in condemning the September 11 terrorist attacks on the US. However, when it came to the formulation of an official government position, the event proved to be the first serious challenge to President Megawati government since she became Indonesia's fourth president in July 2001. Indonesia was once again caught between international necessity on the one hand and domestic political

reality on the other. To that effect, Megawati government was forced to find a balance between US' demands for full-fledged support on its war against terrorism on the one hand, and radical Islamic groups' outcry at home demanding the government to take a primarily anti-US stance on the other.

A Delicate Balancing Act: Indonesia's Government and September 11

In formulating its official stance, Indonesia's government was torn between two conflicting positions. It recognized that Indonesia would soon have to undergo a delicate balancing act. On the one hand, government officials loyal to President Megawati were greatly aware that the horrific event would become a serious international issue with serious implications for the whole world, including Indonesia. In that context, Indonesia might not have many choices but to express its support to the US' call for combating terrorism. On the other hand, it also recognized the need to carefully weight its position against possible domestic reactions, particularly from the Muslim community. To that effect, Megawati government was aware that its support to the US' call for global war on terrorism might be construed at home as an act of submission to the US.

The pressure was strongly felt by Indonesia's government as President Megawati was scheduled to leave for the United States to meet President George Bush on the 19 September, a week after the WTC tragedy. As the date for

her departure was approaching, the situation in Jakarta quickly turned to her disadvantage. Several Islamic groups began to stage protests on the streets of Jakarta, and expressed their anger at the US' accusation of Osama bin Laden as the mastermind of the September 11 attacks; an act they saw as the US' attempt to take Islam as the scapegoat. The timing of Megawati's departure became all more delicate when her Vice-President, Hamzah Haz of the Muslim-oriented United Development Party (PPP), began to express his displeasure to what he saw as an attempt by the US to discredit the Islamic world. He not only resented accusation by the US against the Al-Qaeda and Osama bin Laden but also went to the extent of saying that the attacks "will hopefully cleanse the USA of its sins."¹

President Megawati took off to the US with such domestic political scene at the background. Indonesia's official position was revealed by President Megawati directly to President George Bush during a meeting at the White House on 19 September 2001. She told her host "we mourn with America, that we share your grief and outrage, and that we strongly condemn terrorism in all of its forms and manifestations." She also stressed that "Indonesia is ready to cooperate with the US and other civilized countries on counter-terrorism."²

¹ *Pikiran Rakyat*, 17 September 2001.

² President Megawati Soekarnoputri, address at the gala dinner in Washington DC, held by the

President Megawati also "condemned the barbaric and indiscriminate acts against innocent civilians," and pledged "to cooperate with the international community in combating terrorism."³ In New York, President Megawati called the September 11 as "the worst atrocity ... in the history of civilization."⁴

In return for her support, Washington pledged to continue its support to help Indonesia rebuild its economy shattered by the Asian financial crisis of the late 1990s, and expressed continuing support for Indonesia's difficult transition towards democracy. The most encouraging promise by Washington to the Indonesian government was the pledge to seek for a renewal of military ties between the two countries, which had been disrupted since September 1999, including the promise to lift an embargo on sales of non-lethal military items and the establishment of a bilateral security dialogue. In total, Washington pledged to provide financial aid of US\$657.7 million to Indonesia.⁵

In Indonesia, however, the good news was received with a degree of suspicion, especially within radical

United States-Indonesia Society, 19 September 2001, reprinted in *The Jakarta Post*, 21 September 2001.

³ Joint Statement between the United States of America and the Republic of Indonesia, 19 September 2001.

⁴ *The Jakarta Post*, 1 November 2001.

⁵ *The Jakarta Post*, 22 September 2001.

Islamic circles. Jafar Umar Thalib, the leader of Laskar Jihad, maintained that Megawati's visit to the US "clearly ignored the feeling of the ummah." The visit, he said, "can be seen as a form of support by Megawati to America's plan to attack Afghanistan."⁶ Consequently, anti-American protests grew larger and stronger, especially in response to the reports of the imminent American attacks on Afghanistan. Mass demonstrations against the US were now also staged in several other cities by several Islamic organizations.

The scope of the protests became alarming when several hard-line Islamic groups, such as the Islamic Defenders Front (FPI) and the Laskar Jihad (Jihad Troops) began to warn Americans to immediately leave Indonesia.⁷ They also threatened to use their paramilitaries to "sweep" hotels and other places in search of American visitors. Some even went to the extent of threatening to attack American facilities and interests in Indonesia should the US carry out its plan to attack Afghanistan. Concerned about the growing magnitude of anti-American protests and threats to American interests and citizens, the US Ambassador to Indonesia, Robert Gelbard, filled a request for a security guarantee to the Indonesian Police.⁸ When he felt that the Police

would not be able to extend such guarantee, the US Embassy was forced to close for two weeks.⁹

The most serious development, however, occurred on 25 September when the Indonesia's Council of Ulama (MUI), stated its position. The Council, a semi-official body of Indonesian clerics, issued a declaration calling "on Muslims in the world for *jihad fii sabilillah* (fight in the path of Allah) should the aggression by the US and its allies against Afghanistan and the Islamic world occur."¹⁰ The MUI's Secretary-General Din Syamsuddin, arguing that the aggression towards Afghanistan could be seen as [an act of] hostility and hatred against Islam and Muslims, and as [an act of] injustice, terrorism and a form of imperialism, called on "the US government to reflect on the injustices it has been responsible for and the double standards it has adopted, especially the violations against human rights that have affected the Muslim community."¹¹ Two other important points included in the Council's statement—the condemnation of the September 11 terrorist attacks and its opposition to the planned "sweeping" against American citizens—were understandably overshadowed by the call for *jihad*. In effect, the MUI's declaration of *jihad* was seen as "one of the harshest statements of support for the Taliban heard

⁶See, interview with Jafar Umar Thalib, *Koran Tempo*, 25 September 2001.

⁷*The Jakarta Post*, 22 September 2001.

⁸*Koran Tempo*, 22 September 2001.

⁹*Kompas*, 28 September 2001.

¹⁰*The Jakarta Post*, 26 September 2001.

¹¹*Ibid.*

from any state-sponsored religious body in the Muslim world.”¹²

The pressure intensified with the US finally going ahead with its plan to attack Afghanistan and the Taliban. As anti-US protests now began to pose a challenge to Megawati presidency, on 8 October 2001 the government was forced to produce a six points statement on the issue.¹³ The six points contained in the statement are as follows:

- the government of Indonesia expressed a deep concern that a military act was finally carried out;
- Indonesia noted the statement by American government that the operation is only launched against terrorist training camps and military installations, and that the operation is not meant as an act of hostility against Islam;
- the government of Indonesia hopes that the operation is strictly limited in terms of targets and duration so that it would minimize civilian casualties;
- Indonesia calls on the United Nation to undertake collective response to restore the situation;
- the government of Indonesia warns that reactions and sympathy from In-

donesian society should not be expressed in ways contrary to the law;

- Indonesia would provide humanitarian assistance to ease the suffering of the people of Afghanistan.

Such position, however, angered radical groups in Indonesia, especially due to the fact that the government failed to condemn US military action against Afghanistan. The statement, which stopped short of criticizing the US military campaign, was also seen as a statement of support to the US. Consequently, anti-American protests intensified. Radical groups began to burn American flags and effigy of President Bush. Threats to expel American citizens intensified. In Makassar, South Sulawesi, Japanese flag at its consulate there was hauled down by a group of radical students.¹⁴ Several Islamic organizations began to launch a campaign to boycott American goods and products. Some even began to register volunteers to be sent to join the Taliban government in Afghanistan in their fight against the US. The MUI condemned the US military campaign as “a manifestation of arrogance and oppression,” renewed its call for *Jihad* , and urged the Indonesian government to temporarily freeze its diplomatic relations with the US and its allies.¹⁵

¹²Robert W. Hefner, “Muslim Politics in Indonesia After September 11,” statements before US House of Representatives, at http://www.house.gov/international_relations/hefn1212.htm

¹³See, Statement of the Government of Indonesia on Military Action in Afghanistan, 8 October 2001.

¹⁴*The Jakarta Post*, 10 October 2001.

¹⁵See, *Pernyataan Sikap Majelis Ulama Indonesia dan Organisasi/Lembaga Islam di Indonesia* [Statement by Indonesia’s Council of Ulama and Indonesia’s Islamic Organizations and Institutions], issued in Jakarta, 8 October 2001.

Din Syamsuddin even declared that "the MUI will not bar the Muslims [in Indonesia] from taking up arms to wage *jihād*. That is part of human rights."¹⁶ The call by the MUI that Indonesia should break its diplomatic ties with the US was increasingly voiced by other radical Islamic groups.

Such turn of events clearly put Megawati government on the defensive. Megawati finally bowed to the pressure when, on 14 October at the Istiqlal Grand Mosque in Jakarta, she issued sharp criticisms of the US military campaign in Afghanistan. She declared that "it is unacceptable that someone, a group or even a government —arguing that they are hunting down perpetrators of the terror— attack people or another country for whatever reason." She also maintained that "there are rules that need to be observed. Without observing those rules, the action initially meant to combat violence at the end would itself become a new act of terror and violence" and "blood cannot be cleansed with blood."¹⁷ The speech, especially the criticisms against the US, was widely seen in Indonesia and abroad as a significant departure from Indonesia's previous stance on the issue. As men-

tioned earlier, in its statement on 8 October, Megawati government refrained from criticising the American attack, expressing instead the hope that "the operation is strictly limited in terms of targets and duration so that it would minimise civilian casualties."¹⁸

The next day, however, the police dispersed a major anti-American protest by Islamic Defenders Front (FPI) in front of the parliament building in Jakarta. There was violence on both sides, and more than a dozen people were injured when the police broke up the demonstration. It seemed that the message was clear. The government would not tolerate further threats to social order and its international reputation. Vice President Hamzah Haz, who had been critical of American policy after September 11, by mid-October was toning down his rhetoric and downplaying differences between his own and Megawati's positions.¹⁹ Within days, the sights of anti-American protesters calling for *jihād* quickly disappeared from the streets of Jakarta and other major cities. Habieb Raziq, leader of FPI and the most vocal opponents of American campaign in Afghanistan, began to tone down his rhetoric and now filled a lawsuit against the police, claiming that the police had violated their human rights. He also publicly stated that FPI

¹⁶"Afghanistan Pun Membara" [Afghanistan Is on Fire], *Panji Masyarakat*, 17 October 2001.

¹⁷"Unacceptable, looking for Terrorists by Attacking Other Countries," *Tempo Interaktif*, available at <http://www.tempointeraktif.com/news/2001/10/14/1,1,18,id.html>, accessed on 24 February 2002 at 13.34 pm (Indonesian time). The complete text of the speech available at <http://www.indonesianembassy.org.uk>

¹⁸Statement of the Government of Indonesia on Military Action in Afghanistan, 8 October 2001.

¹⁹"Mega Akhirnya Kecam Amerika" [Mega Finally Condemned America], *Suara Merdeka*, 16 October 2001.

members had not searched for foreigners and would not do so in the future, maintaining that "the issue is only talks."²⁰

Regardless the effects of the speech on the streets in Jakarta, the change of tone in Megawati government's position inevitably attracted some reactions from abroad. A strong criticism was soon directed at Megawati's speech by Australia, a close American ally in the Pacific. Prime Minister John Howard remarked that the speech could bring instability to the Asia-Pacific region.²¹ Meanwhile, the response in Washington was decidedly muted, with some government officials saw the remarks as being "not helpful." White House's Press Secretary Ari Fleischer simply commented on Megawati's criticism by saying that "the best defence [against terrorism] is a strong offense."²² And, unlike PM Howard, US Deputy Secretary of State Richard Armitage downplayed the remarks, saying that he believed that Indonesia would continue to be supportive of the US.²³ However, one American analyst simply labelled Megawati's speech as an instance

of "hypocrisy."²⁴ For others, Megawati's criticism "was largely meant for internal consumption."²⁵ With such differing responses, one can view Megawati's remarks, and Indonesia's changed position, either as an instance of plain hypocrisy or as a form of strategic ambiguity.

Indonesia and the US-Led War Against Terrorism

Despite significant decrease in overt anti-American sentiments on the streets of Jakarta, the Indonesian government continued to stress its opposition to the American military campaign in Afghanistan. Coordinating Minister for Political, Social, and Security Affairs Lt.-Gen. (ret.) Susilo Bambang Yudhoyono, for example, warned that the US-led attacks on Afghanistan could spark a clash of civilization. Yudhoyono feared that "if this conflict widens, then many countries will be destabilized. This will create a new unwanted conflict, for example the West against non-Western countries; the United States versus the rest of the world." He also maintained that despite Indonesia's support to the efforts to combat terrorism, it saw the use of excessive military force by the US as counter-productive.²⁶

²⁰Bill Guerin, "Will Indonesia Leader Please Step Forward," *Asia Times On-Line*, 20 October 2001, at <http://www.atimes.com>

²¹*Pikiran Rakyat*, 19 October 2001.

²²Quoted in "Soal Pernyataan Mega: Syafii Nilai Cukup, Akbar Minta Diformalkan" [On Mega's Remarks: Syafii Said Enough, Akbar Asked to be Formalized], *Suara Merdeka*, 18 October 2001.

²³John Roberts and Peter Symonds, "Megawati Continues Balancing Act in Indonesia," *World Socialist Web Site*, 22 October 2001, at <http://www.wsws.org/articles/2001/indo-022-prn>

²⁴Dana Dillon, "Hypocrisy in Jakarta," at <http://www.heritage.org/views/2001/ed111301.html>

²⁵Roberts and Symonds, "Megawati Continues Balancing Act."

²⁶"Indonesia Warns US of War Between West and Rest of World," *Islam Online.net*, at <http://64.29.210.216/English/news/2001-10/18/article4.shtml>

In late October 2001, President Megawati called on the US to stop its bombings of Afghanistan, especially during the Muslim holy month of Ramadhan and Christmas. Speaking at the opening of MPR Annual Session, she maintained that "prolonged military action is not only counter-productive but also can weaken the global coalition's joint effort to combat terrorism."²⁷ She also stated that "we call for the need for a humanitarian pause to provide an opportunity to handle humanitarian aspects, and to find a way to find a solution via political and diplomatic means."²⁸ She also demanded the US to offer proof that Osama bin Laden was responsible for the September 11 attacks. Megawati reminded the US that "it is an obligation of every party to help find and show to the world the convincing evidence of connection of any elements allegedly involved in these irresponsible actions before taking measures to combat terrorism."²⁹

Indonesia displayed its uneasiness with the US-led coalition against terrorism when Foreign Minister Hassan Wira-

yuda, speaking during the Asia-Pacific Economic Meeting (APEC) meeting in Shanghai, maintained that Indonesia wanted to see the United Nations take the leading role and initiate a collective response in combating international terrorism.³⁰ After a meeting with US Secretary of State Colin Powell on Friday, Foreign Minister Wirayuda stated that his government believes "a collective international response" to the Sept. 11 terrorist attacks is preferable to unilateral US military action.³¹ Indonesia's reluctance to fully become part of an American-led coalition against terrorism was also evident when the US demanded that every country took necessary measures to freeze financial assets of organizations suspected to have links with international terrorism.

Again, domestic political calculation seemed to have played an important role here. For Indonesia, the US' demand, despite backed by UN Resolution No. 1333/2000 and No. 1373/2000, presented the government with a difficult dilemma. As noted by Sheldon Simon, "to scrutinize [Islamic charities] in Indonesia risks a significant Muslim backlash. Moreover, neither the Finance Ministry nor Bank Indonesia is equipped to monitor the thousands of financial transaction coming from overseas to non-

²⁷"Megawati Urges End to U.S. Strikes," CNN.com, accessed on 24 February 2002 at <http://www.cnn.com/2001/WORLD/asiapf/southeast/11/01/megawati.address>

²⁸Ibid.

²⁹Richard C. Paddock, "Indonesian President Urges Halt to U.S. Bombing of Afghanistan," Los Angeles Times, 2 November 2001, at http://www-tech.mit.edu/v121/N56/Indonesia_Prez.56w.html

³⁰"Indonesia Wants U.N. to Lead Fight Against Terrorism," *IslamOnline.net*, 19 October 2001.

³¹"Bush Sells War Versus Terror to Apec," *Manila Times*, 21 October 2001, internet edition, <http://www.manilatimes.net>

governmental organizations."³² The reality on the ground, however, was murkier than Simon has suggested. Even after Indonesia agreed to undertake investigation, after a long delay, responses from Indonesian officials to the request were still marked by a degree of reluctance and resentments. The Governor of Central Bank, for example, responded to the request by saying that it was easier said than done. A Cabinet Minister, Yusril Ihza Mahendra, maintained that "we cannot just freeze those assets unless we have solid evidence."³³

In general, however, Indonesia came to be seen as being not interested in pursuing the issue of terrorism. Some US officials began to criticize Indonesia, accused it of being too slow, and uncooperative.³⁴ An American analyst bluntly stated that "the Americans are keeping a scorecard for what is being done in Asia. Singapore, Malaysia and the Philippines are getting almost-perfect scores for reining in the terrorists.' In contrast, "the Indonesians have got a big fat goose egg for not trying hard enough"³⁵ Pressure on Indonesia "to do more," however, began to mount when an Indonesian national, Fathur Rohman Al

Ghozi, was arrested in Manila for illegally keeping tons of explosive materials. Later, Al Ghozi revealed that he is a member of Jamaah Islamiyah group, which is believed to have maintained closer ties with Al Qaeda.³⁶ Following the arrest of Al Ghozi, Malaysian police also arrested members of Malaysian Militant Group (KMM), in which an Indonesian Muslim cleric, Abu Bakar Baashir, was implicated. He is in fact the leader of Indonesian Mujahideen Council (MMI). Among those arrested in Malaysia, three were known to be Singaporean and four Indonesians.³⁷

Malaysia and Singapore officials are convinced that Abu Bakar Baasir is also the head of Jamaah Islamiyah group. Malaysian authority has long been trying to imprison him on the charge that he was the main figure behind the militancy of KMM movement.³⁸ The KMM is also accused behind the attempt to overthrow the Malaysian Prime Minister Mahathir Mohammad and set up an Islamic state in Malaysia. The KMM was also reportedly involved in the conflict between Muslims and Christians in Ambon by providing money to fund

³²See, Sheldon W. Simon, "Mixed Reactions in Southeast Asia to the U.S. War on Terrorism," *Comparative Connection*, October-November 2001.

³³Interview with Yusril Ihza Mahendra, *Forum Keadilan*, no. 13 (18 November 2001).

³⁴*The Jakarta Post*, 9 January 2002.

³⁵*The Straits Times*, 20 January 2002.

³⁶The Jemaah Islamiyah (JI) is a small but discipline militant groups. It has regional and international networks. Regionally, JI exists in Indonesia, Brunei Darussalam, Malaysia, the Philippines and Singapore. Internationally, it is believed that JI has a very strong relationship with Osama Bin Laden's Al Qaeda.

³⁷"3 Singaporeans among 23 militants held", *The Straits Times*, 25 January 2002.

³⁸"Misteri Kumpulan Mujahidin Malaysia", *Tempo*, 9 September 2001.

the Muslim side in Ambon, which was valued at 225 million rupiah.³⁹

However, Indonesia continues to deny and reject the allegations that "Indonesia was home to groups or individuals who were part of a regional terrorist network."⁴⁰ Government officials also rejected the allegations about the possible links between Indonesian radical groups and international terrorist networks. Apparently, the reason of such denial is that the Indonesian government is worried about the potential backlash from Muslim groups in the country. Such Indonesia's attitude inevitably frustrated and created uneasiness among its ASEAN partners, prompting them to urge Jakarta to take note of security implications of transnational terrorism.⁴¹ When a serious row erupted between Jakarta and Singapore over the remarks by Senior Minister Lee Kuan Yew of the presence of terrorist leaders in Indonesia, the Indonesian attitude is increasingly becoming more puzzling than ever.

THE DOMESTIC BASIS OF AMBIGUITY: THE PRIMACY OF POLITICAL REALITY

Indeed, on the balance, Indonesia's reaction to US' military campaign in Afghanistan, and the subsequent US-led war on global terrorism, bore the marks

of ambiguity. Initially, President Megawati pledged a full support to the US when she was in Washington DC. Later, after the US' attacks on Afghanistan, she became critical of the US' action. Judging from how the events had turned out following Megawati's tough remarks, however, it should be clear that "Megawati's veiled criticism of the US is part of a strategy to contain the protests and opposition."⁴² However, President Megawati's change of position on the US military campaign in Afghanistan still begs a bigger question: why did she backtrack from her previous apparent support to the US-led war against terrorism in Afghanistan? What prompted her to finally modify her government's stance, despite the government's pronouncement earlier that "the government's stance is clear and we are not going to review it..."⁴³

The answers to these questions can be found within Indonesia's domestic political context. Indeed, broader domestic political issues seemed to have set the context for Megawati's changed position. In this regards, two factors are of paramount importance: the Islamic challenge to Megawati presidency, and the fragile nature of her coalition government. Both factors clearly reveal vulnerability of Megawati government to national issues with identifiable Islamic dimension. More im-

³⁹Ibid.

⁴⁰"Terrorist? Jakarta 'yet to see proof'", *The Straits Times*, 22 January 2002

⁴¹*The Jakarta Post*, 2 January 2002.

⁴²Roberts and Symonds, "Megawati Continues Balancing Act."

⁴³"Govt Rejects Calls to Change Stance Over U.S. Attacks" *The Jakarta Post*, 10 October 2001.

portantly, the whole episode highlights the growing significance of Islam in Indonesia's politics and policy-process.

The Islamic Challenge

Indeed, the pressure exercised by radical Islamic groups on Megawati did not start with the September 11 attacks. In fact, it had started since 27 August when thousands of members of FPI launched a demonstration in front of the Parliament (DPR). They demanded the revival of the Jakarta Charter on Islamic law in the 1945 Constitution obliging Indonesia's Muslims to observe *syari'ah* law (Islamic law). The adoption of the Charter by the state, which was dropped from the Constitution on 18 August 1945, is tantamount to a change in the nature of Indonesia's secular state identity into an Islamic state. The pressure became more significant when two Islamic parties —the PPP led by Vice-President Hamzah Haz and the Moon and Star Party (PBB)— officially proposed to the MPR that the Jakarta Charter be adopted in the 1945 Constitution during its Annual Session scheduled to take place in November.

The re-launching of the Jakarta Charter issue was clearly meant to test Megawati government. Those parties that took part in the undertaking were the same parties that opposed and blocked the election of Megawati as president on gender basis back in October 1999. The fact that Megawati is now the president does not necessarily reflect a fundamental change in the attitude of these parties. She became Indonesia's president prim-

arily due to the growing resentments of many Muslim-based parties, especially those grouped under the Central Axis, against President Abdurrahman Wahid. The Islamic parties grouped under the Central Axis were forced to switch their support from Wahid to Megawati. In that context, her position would continue to be secure only if she is able to sustain the political support from Islamic parties within the parliament.

In that context, President Megawati seems to realize that a showdown with her coalition partners over the war on terrorism issue was not worth the effort. As discussed earlier, Vice President Hamzah Haz has been one of the most ardent critic of the US's military actions in Afghanistan. Hamzah's comments on the issue put Megawati in a difficult position *vis-à-vis* the larger Islamic community. He, for example, maintained that "it is our obligation to help Afghanistan because it is a Muslim country" and "the demands of the Muslim people here have been echoed by the government"⁴⁴ Moreover, reports on the growing tension between President Megawati and her Vice-President Hamzah Haz have circulated even before the September 11. It was reported that the decision by PPP to endorse the inclusion of the Jakarta Charter into the 1945 Constitution has created tension in the relationship between the two. It was believed also that the PPP's attempt to raise the Jakarta

⁴⁴*The Jakarta Post*, 15 October 2001 and 3 November, 2001, and *The Straits Times*, 9 October 2001.

Charter issue has revived Megawati's old suspicion that the PPP, her main coalition partner, has not genuinely supported her largely secular government.

The Nature of Megawati Government

The ambiguity in Megawati government's attitude was also related to the nature of her government as a weak government. There have been cases where the government, especially in relations to impacts of the September 11 on the country, was not able to reinforce its owns decision and policies. A cabinet meeting, for example, decided to prohibit excessive demonstrations and acts of violence against foreigners, the burning of foreign flags and foreign leaders effigies, and to prohibit Indonesian citizens from joining foreign military services at war. The decision was openly challenged by the anti-American forces. Instead of deterring them from staging the demonstrations, the decision was defied when the radical groups stepped up their demonstrations and continued to issue threats to attack US citizens on Indonesian soil. And, Megawati government failed to enforce the law when some of the demonstrators did burn American flags and President Bush's effigy in front of American Embassy.

THE PUBLIC REACTIONS: THE DEBATE WITHIN THE ISLAMIC COMMUNITY

If the government's response demonstrates a delicate balance it must strike,

and was generally viewed as a strategic necessity especially in the light of domestic political reality, developments within Indonesia's Muslim community since the September 11 attacks have raised a fundamental question regarding the nature of Islam in the country. With the rise of anti-American protests, accompanied by threats to "sweep" American citizens and threats against American interests, taking place for several weeks, questions began to emerge whether Indonesia's Islam, known for its tolerance and moderate nature, was undergoing a radicalization trend. More specifically, is Indonesia increasingly becoming more anti-American? Is the radical voice increasingly gaining stronger ground in Indonesia?

The general reactions from Indonesia's Islamic community to the September 11 attacks on the US have been those of measured condemnation, if not of ambiguity. On the one hand, several Muslim leaders quickly condemned the attacks as barbaric acts committed by evil people. But, on the other hand, they were also quick in reminding the US to acknowledge that the roots of the problem can be found within American policy towards the Islamic world in general and the Israeli-Palestinian conflict in particular. Some even went to the extent of making comments that could easily be interpreted by the US as condoning the attacks. In other words, the condemnation of the terrorist attacks was often qualified with arguments that American government itself was also partly responsible to what happened. While many Muslim

leaders resented American's accusations that "Islamic" terrorists were behind the attacks, they at the same time were quick in pointing to US support to Israel as the roots of terrorism.

In responding to the US military campaign in Afghanistan, Indonesians of all streams, from traditionalist Islam to secular-nationalists, were almost unanimous in expressing their displeasure at American display of force in Afghanistan. However, when strong and intimidating reactions from militant Islamic groups began to dominate much of domestic and international media coverage, the tolerant image of Indonesia's Islam was soon put under a serious test. That tolerant image seemed to have been overshadowed by voices of anger expressed on the streets of Jakarta, especially in front of American Embassy, by angry Muslims equating American attacks on Afghanistan as attacks on Islam as whole. The image of Islam in Indonesia as a moderate force deteriorated further when leaders of radical Islamic groups threatened to expel foreigners and that a jihad would be waged against the US. Some Islamic organizations even began to recruit volunteers to be sent to Afghanistan to fight along the Taliban side.

The situation worsened when the police seemed reluctant to take lawful actions against such threats. The decision by the US government to authorize a voluntary evacuation of its citizens inevitably lent a greater credibility to such threats. When the voice of mainstream groups within the Islamic community was

not clearly heard, and anti-American protests went on for a few weeks without any challenge from the authorities and other elements of Islamic community, worry grew both in Indonesia and abroad that Indonesia's Islam had been dominated by the radicals, and its moderate face has been radicalized.

In fact, the radicals who took to the streets constitute a minority group within the highly pluralistic Islamic community in Indonesia. Two groups were particularly active in these anti-American protests. The first was the Islamic Defenders Front (*Front Pembela Islam/FPI*), an organization that became infamous after attacking and closing down a number of bars and entertainment places in Jakarta since 1999. The FPI, led by a number of Indonesians of Arabic descents, quickly established itself as a militant Islamic group with more than 20,000 members, mainly in Jakarta and Solo. The second group, the Islamic Youth Movement (*Gerakan Pemuda Islam/GPI*), is also a minor Islamic group comprising mainly militant youth. While the GPI has several branches across Indonesia, only those in Jakarta and few other smaller cities were actively involved in street protests against the US. This group also claimed that it had sent around 300 of its members to fight against the US in Afghanistan. Nevertheless, as attention was disproportionably given to them, their views were presented as if they were the dominant views of Indonesia's Muslims.

Indeed, the media —especially print and visual media— did play a crucial role

in creating such an impression. It failed to capture a broader and more comprehensive picture of the debate within Indonesia's Muslim community. In reality, moderate voices—especially from the moderate and mainstream Islamic organizations, such as the Nahdlatul Ulama (with approximately 38 millions members) and Muhammadiyah (with approximately 28 million members)—had also made their voices clear. However, as the media was often drawn into making anti-American euphoria on the streets as headlines, those moderate voices were often lost.⁴⁵ For example, Chairman of Muhammadiyah, Ahmad Syafii Maarif, had rejected the call for a world-wide *jihad* issued by Taliban rulers on 17 October, should the US attack a Muslim country, warning Indonesian Muslims not “to show emotional ties to the Taliban.”⁴⁶ He also reacted strongly to the call for *jihad* by MUI, saying that “it is unwise and does not bring any good to Indonesia.”⁴⁷ According to Maarif, the *jihad* call “can become the dry grass for a fire.”⁴⁸ He also condemned the “sweeping” against foreigners as “barbaric and uncivilized” and appealed to those demanding the suspension of diplomatic ties with the US “to use their common sense.”⁴⁹

⁴⁵Those moderate voices, strangely, often only appeared in the Internet news sites.

⁴⁶*The Jakarta Post*, 18 September 2001.

⁴⁷*Tempo*, 7 October 2001, p. 21.

⁴⁸*Ibid.*

⁴⁹This comment was reported at <http://www.mandiri.com>, on 11 October 2001.

Moderate views were also expressed by Amien Rais, Chairman of the People's Consultative Assembly (MPR) and also former chairman of Muhammadiyah, whom in the past often seen as “a not-so-moderate” Islamic leader. Responding to the MUI's call for *jihad*, for example, Rais warned Indonesian Muslims of “not to resort to *jihad* so hastily and easily.” He also stated that “I personally do not want to join the bandwagon and inflame the spirit of *jihad*, unless the US launched indiscriminate attacks on Afghanistan without distinguishing civilians and military targets, and extend the war to other Muslim countries *in the name of religion*.”⁵⁰ On the “sweeping” threats, Rais' response was even stronger than other Muslim leaders' when he stated that, from Islamic point of view, such acts are *haram* (strictly forbidden).⁵¹ Responding to the demands that Indonesia should break its ties with the US, he warned that “despite our condemnation of American attacks on Afghanistan, we should not sacrifice the larger national interests of our country.”⁵²

As mentioned earlier, strong criticisms by President Megawati of American attacks on Afghanistan, did improve the domestic situation. The MUI leaders, for example, began to clarify its earlier call for *jihad*, arguing that such a *jihad*

⁵⁰*Kompas*, 28 September 2001. Italic added.

⁵¹*Ibid.*

⁵²Amien Rais, “Kita Memang Lemah” [We Are Seriously Weak], *Adil*, available at <http://www.detik.com>, 8 November 2001.

could be undertaken in many other forms than war. It was at this time that key Muslim leaders from the mainstream Islamic organizations, such as the NU and Muhammadiyah, began to regain dominance in the public discourse, and filled it with more rational and moderate view. Maarif, for example, continued his denouncement of the threats against foreigners and Americans as "uncivilized and barbaric" and argued that Indonesia would not survive its economic crisis without American help. He also disapproved the plan by some Islamic organizations to send volunteers to fight alongside the Taliban in Afghanistan. Others, such as NU Chairman, Hasyim Muzadi, and the President of State Institute of Islamic Studies, Azyumardi Azra, called Indonesian Muslims to focus more on Indonesia's national problems, and worry less about Afghanistan. Demands that Indonesia should break its diplomatic relations with the US were also dismissed as unrealistic and irrational.

By late November, mainstream Islamic forces seemed to have been successful in their attempt to counter the views of the radicals. Even though the US continued its military campaign in Afghanistan well into Ramadhan (the Islamic holy month that started on 17 November 2001), there were no major anti-American protests carried out by radical Islamic groups. The return of the mainstream moderate was further consolidated when top leaders of NU and Muhammadiyah, Syafii Maarif and Hasyim Muzadi, met on 2 January 2002. The meeting was meant to forge a common platform between the two

Islamic groups in addressing serious challenges facing the Muslim community in particular and Indonesia in general. During the meeting, both leaders expressed their concerns of growing Islamic radicalism in Indonesia. They also stressed that the NU and Muhammadiyah, as the two largest Islamic organizations in Indonesia, should ensure that a moderate and tolerant face of Islam would continue to be the mainstream in the country. In doing so, both organizations agreed to pay more attention to radical Islamic groups, and explain to them what a true face of Islam should be.⁵³

CONCLUSION

In terms of domestic political context, the event of September 11 posed the first serious challenge to President Megawati government since it took over Indonesia in July 2001. It soon unleashed a wave of anti-American sentiments that quickly became a formidable constraint to the attempts by Megawati government to accelerate Indonesia's economic recovery at home and restore its international credibility and image abroad. More importantly, it also demonstrates the new dynamics within Indonesia's Islamic community, reinforces the importance of Islamic factor in domestic

⁵³The author participated in the meeting, as a member of Muhammadiyah's Central Executive Board. He has also been assigned by Syafii Maarif to represent Muhammadiyah in the Muhammadiyah-NU Joint Task-Force charged with the task of formulating a Plan of Actions for the program.

politics, and exposes the vulnerability of Megawati government to national issues with identifiable Islamic dimension.

The government, however, managed to tone down the pressure by, first, becoming more critical of the US' attacks on Afghanistan, and second, by taking stern measures against demonstrators. Sterns measures taken by the police against the demonstrators on 15 October might have discouraged the demonstrators and forced them to consolidate. More importantly, the success of Northern Alliance forces in driving the Taliban has also reinforced the image that the war in Afghanistan is one between Muslim groups rather than between the US and the Muslims. And, the critical stance displayed by President Megawati against the US attack on Afghanistan was widely welcome not only by anti-American forces in the country, but also by others within the political elite. In this case, the dynamics within Indonesia's politics, marked by the growing importance of Islam and the weak nature of Megawati government, primarily contributed to the change in Megawati's position on the issue.

The whole episode, therefore, clearly demonstrates a degree of uneasiness among Indonesian elite to be associated with the US-led war on Afghanistan. In fact, in order to create a sense of in-

dependence in the eyes of the Islamic constituency, the Indonesian government is also reluctant to be seen as part of a US-led global war against terrorism. It wanted to move on its own pace and terms. However, in light of recent developments both in Southeast Asia and the world, and also due to the nature of the problem, the future path for the Indonesian government on this front might not be an easy one.

The situation within the Islamic community, however, began to show a more encouraging trend. The moderate voices within Indonesia's Islam have now returned to the main stage. The problem of religious radicalization, however, remains one of the most intriguing issues in the country. As correctly noted by Hefner, "rather than reflecting broad public sentiment, however, extremist statements like those calling for jihad against the US have more to do with a bitter struggle now unfolding between moderates and hardliners for the hearts and minds of the Muslim community."⁵⁴ Even though that struggle is far from over, there are reasons to believe that Indonesia would remain a force that represents a moderate face of Islam in the years to come.

⁵⁴Hefner, "Muslim Politics in Indonesia."

Indonesia's External Trade and Competitiveness: Assessing the Economic Costs of Terror*

William E. James

INTRODUCTION

THERE is little doubt that the events of 11 September 2001 and apprehensions regarding the security situation in Indonesia in the wake of the terrorist attacks and the launching of allied military operations in Afghanistan have had a negative impact on Indonesia's trade and competitive position. The quantitative analysis of the economic costs of terrorism is a complex task that goes well beyond the scope of this paper. The fact that recessions had already begun in both of

Indonesia's major export markets - USA and Japan — before the attacks took place makes it extremely difficult to infer the extent to which each of these events is to blame for the subsequent downturn in exports (and imports). The volatility of exchange rates and world prices of commodities that Indonesia exports further muddy the water. Hence, rather than attempting to quantify or isolate the impact of the particular events that have occurred, an attempt is made to qualitatively assess how the terrorist attacks and related events may have influenced the external trade and competitiveness of Indonesia using the most recent available data.

*This paper has been prepared for the joint USAID-CSIS Conference on "The Economic Cost of Terrorism: Indonesia's Responses," 7-8 May 2002, in Jakarta. The figures reported herein are preliminary and subject to revision. These data, compiled by the author from a variety of sources, where possible are in common units using the IMF period average exchange rate. This views expressed herein are those of the author and not necessarily those of USAID or the Indonesian government.

The deterioration of the external economic situation facing Indonesia in the year 2001 compared with 2000 was apparent even prior to the September 11 attacks. The United States' decision to strike back at the culprits and to launch a more general global campaign against terrorism put Indonesia in a delicate

position. Indonesia was presented with a clear political choice in responding to these events in an already difficult economic environment. The choice to actively join or not to join in the fight against terrorism carried weighty economic consequences for Indonesia. The decision to respond positively, if tentatively at first, to the call to combat global terrorism was welcomed by the United States and, generally, by the international community. Economics clearly played an important role in Indonesia's decision, but this is not to suggest that only economics was the driving factor.

The economic consequences of a failure to respond as Indonesia did would have been quite serious. By choosing as it did, the government of Indonesia has subsequently been able to successfully negotiate debt rescheduling under the generous terms of the Paris Club III with positive implications for the fiscal budget. The improving fiscal situation, brought about by reduced subsidies on fuel, electricity, basic telephone services and public transportation, coupled with successful asset sales (Bank Central Asia in particular) has helped to reduce upward pressure on interest rates and reverse downward pressures on the exchange rate. In turn, stock prices have rebounded and, although year-on-year inflation is still running high through April (13.3% year-on-year), the rate of inflation rate has finally eased after accelerating in the first two months of 2002. Whether or not one thinks the inflation target of 9-10% for CY2002

is obtainable, base money growth has decelerated and is well below the indicative target. The macroeconomic economic situation has begun to turn for the better. This improvement would have been almost inconceivable if Indonesia had made the choice not to participate in the global campaign against terrorism.

Indeed, if Indonesia had chosen to turn its back on the global alliance to combat terrorism, it is very conceivable that the macro situation would have worsened. And it remains conceivable that unless Indonesia takes the path of strengthening its commitment to the global effort to eradicate terrorism, there could be negative near term impacts on exports, investment, tourism, the exchange rate, prices and the budget.¹

This paper examines the impact of the world economic downturn, particularly the recessions in the US and Japan, on Indonesian trade in a comparative perspective. It also addresses the US economy's recovery prospects and the prospects for recovery of world economic activity in 2002 and the implications for Indonesia. In addition, it identifies new challenges facing Indonesia and the implications of Indonesia's stance on the fight against

¹The question of how events will influence world oil prices is of obvious importance in determining the outcome for Indonesia as a net oil exporter. However, the focus of this paper will be on the non-oil economy, leaving the oil price issue to other analysts at the seminar.

Table 1

INDONESIA: NON-OIL EXPORTS TO JAPAN AND USA
(in US\$ million)

	Q1	Q2	Q3	Q4	Q1-Q4
Japan	1,917.1	1,736.3	1,617.3	1,352.8	6,623.5
% Change*	13.42	-4.95	-13.51	-32.8	-10.48
USA	1,880.0	1,972.3	1,929.1	1,444.7	7,226.1
% Change*	7.31	-5.45	-14.97	-9.2	-8.10

*Year-on-year growth comparing the period in 2001 with the same period in 2000. These data are all in current prices.

Source: BPS, *Buletin Ringkas and Berita Resmi Statistik*, various issues.

terror in withstanding these challenges and finally, the paper concludes with some policy implications for Indonesia.

THE GLOBAL SLOWDOWN

Major markets for Indonesian products experienced deteriorating growth as the year 2001 progressed. The entry of the US, Japan and European countries such as Germany into a synchronized recession had sharply reduced global demand for Indonesian exports. Japan, the number one market for overall exports and the second largest market for non-oil exports, reported first quarter growth of just 0.2%, revised second quarter growth is -0.7%, with third quarter growth estimated to be -0.5%. In the fourth quarter, GDP fell again so that growth for the year 2001 was -0.5%.² Japan's third recession in a decade is

the most serious as GDP had never before contracted for three consecutive quarters since Japan revised its method of calculating GDP in 1980.

In the United States GDP growth fell to 0.3% in the second quarter (revised upward from 0.2%) from 1.3% in the first quarter, and growth in the third quarter became negative (-1.3%), the weakest performance in ten years.³

The impact of the recessions on the non-oil export data from the Central Statistical Agency of Indonesia in the Table 1 above is clear.

in constant local currency prices whereas trade growth rates are calculated on the basis of exports and imports of goods in current US dollar prices. Hence, one cannot infer income elasticity of demand from these data.

³The National Bureau for Economic Research (NBER), announced that the US economy entered recession in March 2001, based upon somewhat different criteria than the standard two quarters of zero or negative growth. The NBER assessment is based upon rising unemployment, declining industrial production, personal income and wholesale and retail trade.

²Note that economic growth rates are calculated based on gross domestic product

As income growth has become negative in Japan and the US, and stagnates in the EU, the outlook is bleak across Indonesia's main export destinations. The downturn in the economies of the US and Japan had a severe impact on non-oil/gas exports in 2001 in both key markets. In order to obtain a complete and accurate picture of the downturn's impact, comparison of import data from the two main Indonesian markets with data in Table 1 above is instructive.⁴

The growth of non-oil/gas imports from Indonesia in the US and Japan sharply deteriorates as the year 2001 progresses mirroring the Indonesian export data although the magnitude of decline is smaller using the import data. Growth rates, calculated for each quarter of 2001 and for the year based on official import data from US and Japanese sources, provide a clear picture of the impact of the recessions (Table 2). Weakness in consumer demand in the US and Japanese economies began to take its toll in the second quarter of 2001. U.S. import statistics present a picture that is broadly consistent with

the Indonesian export data.⁵ Growth in demand for Indonesian products has taken a turn for the worse: 11% growth in the first quarter, -1.0% growth in the second quarter, -7.8% growth in the third quarter and -10.8% growth in the fourth quarter.⁶ Import data from Japan (converted into US dollars) reveal a similar picture: 10.4% growth in the first quarter, -0.5% in the second quarter, -3.8% in the third quarter and -21.1% in the fourth quarter. The third and fourth quarter declines in imports from the rest of ASEAN in the US and Japan were sharper than Indonesia. However, imports from China held up much better in the final two quarters in both the US and Japan.

It is important to note that the composition of imports from Indonesia in the US and Japan differ considerably.

In Japan, a much higher proportion of imports (nearly 60%) are primary products and processed resource-based industrial goods. In 2000, base metal and ores, wood and wood products and fishery products alone accounted for 50% of Japan's imports from Indonesia.⁷ In contrast, in the United States,

⁴For a variety of reasons, import data from partner economies may differ from the export data of the source country. For Indonesia, one of the most important differences arises from the use of Singapore (and to a much lesser extent, Hong Kong) as a transshipment center. Indonesian statistics do not distinguish between exports retained by Singapore and re-exports and Singapore does not publish its trade statistics with Indonesia.

⁵As Indonesian export data become available in detail, the author will check their consistency with US import data.

⁶Data compiled by PEG consultant Peter Minor from US sources.

⁷These figures are derived from official sources. See William E. James, "The Competitiveness of Indonesian Non-Oil Products in Major Markets: Market Shares in the United States and Japan," Partnership for Economic Growth, Jakarta, March 2002.

Table 2

GROWTH RATES OF US AND JAPANESE IMPORTS
(2001 vs. 2002, quarterly and annual growth in %)

From Indonesia

	Q1-Q1	Q2-Q2	Q3-Q3	Q4-Q4	Annual 2001
US	11.0	-1.0	-7.8	-10.8	-2.7
Japan	10.4	-0.5	-3.3	-21.1	-4.4

From China

	Q1-Q1	Q2-Q2	Q3-Q3	Q4-Q4	Annual 2001
US	12.8	2.1	-1.3	0.3	2.7
Japan	15.8	7.5	1.8	-6.8	3.8

From ASEAN (Excluding Indonesia)

	Q1-Q1	Q2-Q2	Q3-Q3	Q4-Q4	Annual 2001
US	1.3	-12.1	-24.3	-19.7	-14.6
Japan	7.3	-4.9	-16.5	-26.2	-10.8

Source: US Department of Commerce Imports of Merchandise Trade CD-ROM; Jepang, Ministry of Finance homepage: <http://www.mof.go.jp/english/1c015fle.htm>

primary products and those of resource-based industries comprised less than 20% of imports from Indonesia in 2000.

Manufactured products, chiefly in labor-intensive industries, accounted for the lions' share of imports. Textiles & apparel (24%) and footwear (7%) were among the largest US imports from Indonesia in 2000. The implication of this difference is that Indonesia faces much greater competition from a broader range of producers for its products in the US market than it does in Japan. Any developing country with abundant labor may compete with Indonesia in the US market in labor-intensive manu-

factured products, however, only a few countries possess similar stocks of diverse natural resource wealth as Indonesia and so there are fewer competitors facing Indonesian products exported to Japan.

The unprecedented events of September 11 in the United States have had a strong negative impact on demand for Indonesian products. Buyers have reportedly been unwilling to travel to Indonesia and have begun to source purchases elsewhere in the region. In part, this is a result of the perception that foreigners, particularly Americans, may be targets of extremists and the

issuance of threats against American interests has reinforced this negative image of Indonesia. Indirect evidence of the negative impact of the September 11 attacks is seen in the fact that growth rates of US imports of nine of the ten top labor-intensive-product groups from Indonesia were negative in the fourth quarter of 2001. In seven of nine cases, growth became negative, or if already negative, worsened in the fourth quarter compared with the third quarter of the year. These products include apparel items (5 SITC 3-digit product groups), footwear, and toys and sporting goods.⁸ The downside of the terrorist attacks of September 11 are likely to be magnified should Indonesia be unable to respond effectively to reverse these negative perceptions in the us.

Germany technically entered a recession, with contractions in the second through the fourth quarter. Growth for the year 2001 as a whole was insignificantly 0.5%. In other countries of Europe such as the UK, growth has also begun to slow. Growth in Italy and France became negative in the fourth quarter of the year compared with the previous quarter. Overall, growth in countries in the Euro Zone was estimated to be 1.5% in 2001.⁹

Hong Kong, Taiwan and Singapore recorded negative real economic growth in 2001. Taiwan's recession is the deepest it has ever experienced, with three consecutive quarters of negative year-on-year growth beginning with the second quarter of 2001. Hong Kong had negative growth year-on-year in both the third and fourth quarters of 2001. In Singapore, GDP contracted by 2.2% in 2001. Korea managed to record 2.8% positive GDP growth for 2001, but the outlook for 2002 remains clouded with uncertainty.

Revised global economic growth forecasts reflect the expectation of a prolonged recession. For example, the IMF forecast was revised downward in October 2001 from that of May and indicated that world income will grow by less than 3.0% in 2001 and by only 2.4% in 2002.¹⁰ Slower growth in world income would result in further weakening of demand for Indonesian exports with potentially serious impacts on economic growth in 2002. The forecast for growth of real GDP in developing countries is 4.4% in 2002, led by Asia with a respectable 5.6% growth (led by China and India).

Overall, Indonesian exports (including oil and gas) growth in the year 2001 fell by 9.8% compared with the year 2000 (US\$56.04 billion vs. US\$62.12

⁸James. *ibid.*

⁹Data for the 15 member countries of the EU trade with Indonesia have not been compiled as of the time of writing of this paper.

¹⁰The revised IMF projection of US growth in 2002 is 0.7% indicating that the recession was expected to continue into the first two quarters of 2002.

billion).¹¹ Non-oil/gas exports declined by 9.1% during 2001 compared with 2000 (US\$43.41 billion vs. US\$47.76 billion). The growth in oil and gas exports was -12.09% in 2001. Both agricultural (-9.3%) and manufacturing (-11.1%) exports have declined while mining exports have risen sharply (18.7%) during the year. Indonesia's export performance has held up better than a number of other East and Southeast Asian economies (see the Table 3 below). One reason for this is that Indonesia is less dependent on electronics for exports than many of the neighboring countries. For example, in Taiwan, electrical machinery and equipment made up 56% of merchandise exports in 2000 and exports in this sector alone declined by almost 20% in 2001. Relying heavily on electrical machinery and equipment, Singapore, Malaysia, the Philippines, and Korea experienced export growth that contracted sharply during the year.

National statistical agency's reports around the region reflect the deepening economic slowdown. For example, a comparison of the January-December period compared with the earlier months of the year finds that in all cases export growth fell in the nine economies reported upon in the Table 3 below.¹²

¹¹Exports are on an FOB basis, while imports are on a CIF basis unless otherwise noted.

¹²Two previous reports for growth during the first seven months of 2001 and the first nine months of the year may be requested

Table 3

COMPARISON OF INDONESIAN EXPORT PERFORMANCE WITH ASIAN ECONOMIES

Country/ Territory	Export Growth	
	2001 (y-o-y, % change)	Period
Hong Kong	-2.6 (-11.0*)	Jan.-Dec. 2001
China, Mainland	6.3	Jan.-Dec. 2001
Indonesia	-9.8	Jan.-Dec. 2001
Korea	-13.0	Jan.-Dec. 2001
Malaysia	-10.0	Jan.-Dec. 2001
Philippines	-15.6	Jan.-Dec. 2001
Singapore	-11.8 (-16.2*)	Jan.-Dec. 2001
Thailand	-6.4	Jan.-Dec. 2001
Taiwan	-17.1	Jan.-Dec. 2001

*Domestic exports (excluding petroleum in the case of Singapore).

Source: Author's compilations from national statistical agency home pages for Taiwan, Singapore and the Philippines, from national trade ministries for Korea, Malaysia, Thailand and Hong Kong and from the US-China Business Council for Mainland China. For Indonesia data are from the Central Statistical Agency home page, *Berita Resmi Statistik*, 1 January 2002 and Ministry of Industry and Trade.

In Hong Kong, growth of domestic exports was -11% over the calendar year of 2001 compared with 2000. Overall export growth was helped by the fact that re-exports (mainly of goods from Mainland China) held up better than domestic exports. Despite the relatively mild contraction of re-exports over the year (-1.5%), the decline

from the author: "Indonesia's Export Performance and the Global Economic Slowdown: A Comparison with other East and Southeast Asian Economies," 14 September 2001 and "Indonesia's Export Performance and the Global Economic Slowdown: An Update for the Period January-September 2001," 14 November 2001.

became pronounced starting in September at -9.5%.

In the region, China stands out as the only country that has sustained positive export growth in 2001, although indications (such as the decline in re-exports in Hong Kong noted above) are that growth there slowed significantly as the year progressed. For example, China's export growth slowed from almost 15% in the first quarter to 8.8% for January-June and 6.1% for January-September. However, surprisingly, growth for January-December was 6.3%, indicating fourth quarter performance was relatively good.

In markets in the region, with the exception of the Republic of Korea, there has been a decline in demand for Indonesia's non-oil exports in 2001. Although some Asian countries are moving to fiscal stimulus, including Taiwan, Malaysia, Singapore and Thailand, this may not be enough to lift demand for imports in these markets until the second half of 2002.

China's positive export growth performance matched positive import growth during the year (see Table 4). However, Indonesian non-oil/gas exports to China recorded -9.4% growth in 2001 (year-on-year).¹³

¹³BPS reports a fall in non-oil/gas exports to Singapore in the first nine months of 2001 with a drop in value of over 17%. As Singapore does not publish data on trade with Indonesia, it is not possible to sort out the actual amounts that have Singapore as the ultimate destination of goods exported from Indonesia.

Table 4

**COMPARISON OF IMPORT GROWTH
IN ASIAN ECONOMIES**

Country/ Territory	Export Growth 2001 (y-o-y, % change)	Period
Hong Kong	-5.4	Jan.-Dec. 2001
China, Mainland	8.6	Jan.-Dec. 2001
Indonesia	-8.1	Jan.-Dec. 2001
Korea	-12.0	Jan.-Dec. 2001
Malaysia	-9.9	Jan.-Dec. 2001
Philippines	-5.9	Jan.-Dec. 2001
Singapore	-14.4*	Jan.-Dec. 2001
Thailand	-0.6	Jan.-Dec. 2001
Taiwan	-23.4	Jan.-Dec. 2001

*Non-oil imports.

Source: Author's compilations from national statistical agencies' home pages.

Imports in the East Asian region have started to follow exports with the downturn (Table 4). Growth of imports started to deteriorate sharply in the second quarter of 2001 and this trend appears to be worsening with the latest reports in the third and fourth quarters showing double-digit negative import growth across much of East Asia. For example, import growth in September 2001 (compared with the same period in 2000) was -34.1% in Taiwan and -12% in Korea. In October, negative growth in imports of -21% in Taiwan and -18% in Korea reflect weakening demand as well. In November 2001, import growth was -19% in Korea and -34% in Taiwan. Finally, in December imports growth (year-on-year) was -14% in Korea and -18% in Taiwan.

Additional analysis of Indonesia's export performance may shed some light on the vulnerability of non-oil/gas exports to the global slowdown. With the deteriorating external environment, one expects that the decline in export growth may accelerate. Indonesia's export performance clearly deteriorated over the course of the year as income growth has declined in major markets. Second quarter growth of total exports dropped to -5.1% compared with positive 5.1% growth in the first quarter as external demand continued to weaken. For non-oil/gas exports the growth also became negative in the second quarter (-7.4%) after posting positive 3.6% growth in the first quarter. In the third quarter non-oil/gas exports grew (year-on-year) by -12.6% and in the final quarter by -18.9%. Underlying the declining growth performance is weakness in prices of the products Indonesia exports rather than falling volumes, though there is substantial variance between industries and commodity groups. The diversity of Indonesian exports (including some that are relatively demand inelastic) helped sustain overall performance. Certainly, the lower reliance on electronics as an export in Indonesia relative to neighboring countries has shielded it from a more severe downturn. Consumers in markets for basic commodities may substitute away from expensive brands and items to less expensive ones as their expected real income falls and this may create some opportunities for Indonesian producers to increase their market share.

Indeed a new study of market share of the top 50 Indonesian products in the two major markets of Japan and the United States for the year 2001 indicates this may be the case. In the US, despite contraction in imports in 28 of the 50 product groups, Indonesia increased its share of US imports in 24 cases, had no change in 8 product groups and lost market share in 18. In Japan, there was also a decline in import demand in 28 of the 50 product groups. Indonesia gained market share in 30 product groups, had no change in 4 and lost market share in 16 product groups. Although these data are partially reassuring, there are signs that competitive pressures are mounting on key Indonesian industries, including footwear, apparel, textiles, and wood products. Among the top competitors are China and countries with which the US has entered into free trade agreements, particularly Mexico and Canada.¹⁴

As was the case with exports, Indonesia's growth in imports is slowing as the year progressed and was much lower in the second quarter compared with the first three months of the year. In part, import growth in the first half of the year reflected the recovery and pent-up demand resulting from the crisis in previous years. One can see the drop off in import growth

¹⁴William E. James, "Competitiveness of Indonesian Non-Oil Products in Major Markets: Market Shares in the United States and Japan," 11 March 2002, Jakarta: Partnership for Economic Growth.

Table 5

**INDONESIA: EXPORT AND IMPORT PERFORMANCE IN 2001,
QUARTERLY DATA IN CURRENT PRICES**

(in US\$ billion, % change)

	US\$ billion				% change			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Total exports	14.87	14.43	14.37	12.29	5.1	-5.1	-14.2	-23.3
Non-Oil/Gas	11.18	11.15	11.30	9.72	3.6	-7.4	-12.6	-18.9
Oil & Gas	3.75	3.29	3.07	2.58	10.0	3.4	-19.2	-36.0
Total Imports	9.21	8.54	7.00	6.04	40.5	17.8	-25.3	-41.9
Non-Oil/Gas	8.02	7.20	4.29	4.92	51.6	23.9	-24.6	-44.5
Oil & Gas	1.20	1.33	1.71	1.52	-5.7	-3.5	-8.1	-0.7

Note: Growth are calculated as year-on-year changes, i.e., Jan-Mar of 2001 compared with Jan-Mar 2000.

Source: Ministry of Industry and Trade and Central Statistical Agency.

rates from strong growth in the first two quarters to sharply negative growth by the third quarter. In the fourth quarter imports have contracted by over 40% compared with the same period in the previous year.

PROSPECTS FOR RECOVERY OF THE US ECONOMY

Growth in the fourthquarter of 2001, initially estimated to be 0.2%, was surprisingly 1.4%. There are other signals that the US economy is entering into a recovery phase, including continued high productivity growth (3.5% in the fourth quarter and around 1.7% for the year). Inflation remains muted and the US dollar has strengthened against the Euro and the Yen. Aside from some risk of a "double-dip" recession, however, evidence of a recovery is mounting.

Interest rate cuts and tax reductions in the US helped to stimulate consumer demand and to cushion the pressure of firms and industries as they reduced inventories and cut back production. US consumer confidence, already down because of the stock market correction and rising unemployment, was severely shaken by the September 11 attacks. However, confidence appears to have begun to recover according to surveys of consumers conducted by the University of Michigan. The latest survey for March reports a higher than expected index of confidence and reflects the 5th increase in the past six months. Consumer spending has held up with purchases of autos and housing rising. Another reason for consumer resilience in the US market is that inflation has been falling steadily from an annualised rate of 3.2% in June of 2001 to just 1.1% in January of 2002.

This has helped sustain real incomes despite the job losses and adverse wealth effects of the stock market declines.

OUTLOOK FOR 2002

For the year 2002, a number of countries in the region had projected negative growth of exports and imports during the first two quarters, but expected second half growth to rise sharply. This pattern based, in part, upon the expected pattern of recovery in the United States, maybe unduly pessimistic. Most of the negative growth in current dollar amounts has been due to falling commodity prices, export volumes have actually been increasing. The expectation of a continuation of the US recession into the first and second quarter of the year appears to have been mistaken. Federal Reserve officials and others, including Fed Chairman Alan Greenspan have acknowledged that the economy is already entering the recovery phase. Recent data confirm that industrial output rose by 0.2% in January 2002 and by 0.4% in February (compared with the previous month). Industrial output still remained over 4% below last year's level in 2002 in the first two months, but the month-on-month increases indicate recovery is at hand.

The first quarter of 2002 GDP numbers were very good at 5.8% year-on-year growth. The surge in production was caused in large part by inventory investment as firms began to restock after running down in-

ventory levels during 2001. This recovery may not be as robust as previous recoveries, with growth at about 3% only in the second half of 2002. Typically, recoveries usually achieve around 5 or 6% growth during the first year, but it is unlikely that the first quarter performance will be sustained unless private capital formation accelerates rapidly for the rest of the year.

Prospects for Indonesian exports in the New Year improve with the early recovery in the US, but diminished with the expectation that the recovery would be sluggish after the first quarter. The likelihood that Japan will not soon escape from its economic difficulty, and more intensive competition from producers seeking to aggressively increase exports and penetrate markets also cloud prospects for Indonesia.

There are some possible signs of "bottoming out" as domestic exports of Singapore (-4.1% in January 2002) declined by less than expected and was less than the -16.7% recorded in December of 2001. Similarly, in Korea the January 2002 contraction in exports (-8.9%) was less than expected and lower than the actual decline of -19.6% in December 2001. This was also the case for Taiwan where exports (-1.4%) also fell less than expected and less than in the previous month. However, fourth quarter trade figures are not reassuring and indicate a continuation in the downward trend. For example, export growth in Korea was -20% in December 2001 and import

growth was -14%. And while January export data came in better than expected for Korea, exports for the month of February 2002 performed poorly, indicating that it is advisable to await first quarter numbers before reaching any conclusions.¹⁵

China's export growth accelerated in January-February 2002, up by 14.1% year-on-year. In the case of the US market, China's exports rose by 18% during this period. Hence, it is likely that China will continue to set the pace in Asia in terms of export performance in the coming year, particularly given the improved market access it is starting to enjoy as a WTO member.

The outlook is further complicated by three factors: (1) the sharp depreciation of the yen against the US dollar; (2) the entry of China into the WTO; and (3) the initiation of discriminatory preferential free trade agreements by many of Indonesia's most important trading partners.

Assessing the impact of each of these three factors is rather complex. For example, the yen's decline results in reduced import demand in Japan but also lowers the cost of imported Japanese components used in Indonesian export industries.

¹⁵The first two months of the year provide an unsatisfactory basis for making any firm statements about export recovery because of strong seasonal factors, particularly the shortened number of workdays due to New Year holidays in these months.

In the case of China's WTO entry, there are also complexities in the sense that China will open its markets for agricultural commodities and manufactures of interest to Indonesia but will also enjoy better terms of market access in key sectors in both the United States and the EU. For example, in textiles and apparel China's export growth was constrained in volume to 1% quota growth in the US market until 1 January 2002. From now on, however, China will receive full benefits from the quota liberalization in the US and EU under the Uruguay Agreement on Textiles and Textile Products.

In assessing the impact of new free trade agreements one must distinguish trade creation effects from those of trade diversion — an inherently difficult task *ex ante*. The best way to assure the minimization of trade diversion is to push forward multilateral negotiations for overall trade liberalization in the WTO Doha Round.

In addition to the uncertainties in the international economy, Indonesia faces many domestic problems and challenges that may influence its ability to produce and compete in the international market place. One problem in this regard is that Indonesia is an outlier in terms of domestic price inflation and this will undermine Indonesian products competitiveness, all other things equal, in foreign markets.

Inflation appears to be closely associated with growth in base money and also with depreciation of the cur-

Table 6

**CONSUMER PRICE INFLATION
IN EAST ASIA ECONOMIES**
(y-o-y, % change)

Country/ Region	2000	2001
Hong Kong	-3.8	-1.6
China	0.4	1.1 (Jan.-Jun. 2001)
Korea	2.3	4.1
Indonesia	9.4	12.6
Malaysia	1.6	1.4
Philippines	4.4	6.0
Thailand	1.6	1.6
Taiwan	1.3	0.0

Source: Compiled by the author using national statistical agencies' publications and home pages.

rency. Administered prices of items such as fuel, electricity, public transportation, and volatility in food prices add to inflationary pressures. However, studies by Bank Indonesia and by the IMF show that even after stripping away these volatile elements, so-called "core inflation" remained in double digits in 2001 and in the first quarter of 2002.

CONCLUSION

Trade data for the first quarter of 2002 show a mixed picture in the region. For example, export growth in Hong Kong was 2.2% in March 2002, marking the first increase in 13 months. In Korea, first quarter growth of exports was negative, though March exports declined by far less (-5.7%) than in the first two months (-12.9%) and recorded growth of 9.3%

in April. In Thailand and Vietnam, export growth was also negative in the first quarter. However, the negative growth reflects declining world prices of commodities rather than declining volumes of exports.

Indonesian export data from the Central Statistical Agency for the first quarter of 2002 indicate negative growth (year-on-year) for total exports (-13.9%) and for non-oil exports (-9.6%). However, growth in non-oil exports in the first quarter of 2002 compared with the fourth quarter of 2001 reached 3.4% and for total exports was 1.3%, indicating a turnaround is likely. Data on imports, however, are cause for concern if the numbers are correct.¹⁶ Import data for the first quarter of 2002 indicate year-on-year growth of -30.7% (total) and for non-oil products of -36.8%. These numbers are hardly consistent with an economy growing at a real rate of over 3%! However, quarter-on-quarter growth of non-oil imports is 5.2% and for total imports is 5.8% (comparing the first quarter of 2002 with the last quarter of 2001). Import data for capital goods for the first quarter of 2002 compared with the same period in 2001 indicate growth of -37.5%. These figures do not

¹⁶The existing of rampant smuggling, under-invoicing and false classification of imports may lead to gross understatement of the level of imports. Reconciliation of Indonesian import figures with export figures of partners is difficult, as Singapore, the third largest trading partner, does not publish statistics on trade with Indonesia.

provide much optimistic news about capital formation.

Inflation data (CPI) for April (-0.24% compared with the previous month) and 13.3% year-on-year for the first four months of 2002 compared with the same period in 2001. Inflation is decelerating, reflecting slower growth in base money since the second half of 2001, and the recent appreciation against the US dollar will also help moderate inflationary pressure. On the other hand, increases in fuel prices will add somewhat to headline inflation measures during the course of the year. The positive effects of reducing fuel subsidies on the budget over the course of the year will have enormous benefits in keeping the deficit within bounds.

Progress in asset disposal, along with the Paris Club III rescheduling, will also reduce budgetary pressures. The combination of a stronger currency, reduced budget deficit and moderating CPI inflation indicates that macroeconomic conditions are improving. Thus, cautious optimism is warranted, provided the government can continue to make progress in legal reform and in institutional reform (such as in cleaning up the Customs and Tax Departments).

On the trade front, Indonesia will face the challenge of coping with the great changes that are taking place in the global trading system. For Indonesia, the most immediate challenge comes from China's entry into the WTO. Particularly, in textiles and textile products (Indonesia's most important export industry in terms of employment, non-oil exports and manufacturing production), the China challenge appears to be huge. Data from the US, where China is no longer constrained to 1% quota growth per annum, indicate huge leaps in China's market share relative to other competitors, including Indonesia. The reasons underlying the shifts in market share in textiles and textile products (apparel) in the US, Japan and Europe should be carefully analyzed in order to rectify any shortcomings in present policies.

All in all, Indonesia can ill-afford the adverse impact that association with extremism and terror will have on its image and on the perception of potential buyers and investors. Hence, attention to measures to combat extremism and terrorist groups coupled with strenuous reforms will be essential for strengthening the ability of Indonesian producers to compete in the international markets.

OECD Standards on Money Laundering and Terrorist Financing*

Jerry W. Rowe

INTRODUCTION

RECENTLY the People's Legislative Assembly of Indonesia enacted a money laundering law to address the large amount of proceeds generated by serious crimes committed in Indonesia as well as outside of its borders. This law incorporates many of the recommendations that have been developed and issued by the Financial Action Task Force (FATF), an intergovernmental body created by the G-7 in 1989 for the purpose of developing and promoting policies to combat money laundering.

This paper discusses the recommendations of FATF and offers insight into the next phase of combating money laundering and terrorist financing in Indonesia.

*This paper was presented at the conference on "The Economic Cost of Terrorism: Indonesia's Responses", held in Jakarta, 7 May 2002. The conference was organized by CSIS with the support of USAID.

MONEY LAUNDERING

With few exceptions, criminals are motivated by one thing — profit. Greed drives the criminal, and the end result is that illegally gained money must be introduced into the nation's legitimate financial systems.

Money laundering generally involves a series of multiple transactions used to disguise the source of financial assets so that those assets may be used without compromising the criminals who seek to use the funds.¹ These transactions typically fall into three stages: (1) Placement, the process of placing, through deposits, wire transfers, or other means, unlawful proceeds into financial institutions; (2) Layering, the process of separating the proceeds of criminal activity from their origin through the use of layers of complex financial

¹International Narcotics Control Strategy Report March 2001, "Money Laundering and Financial Crimes", <http://www.state.gov/g/inl/rls/nrcpt/2001/rpt/>

transactions; and (3) Integration, the process of using an apparently legitimate transaction to disguise the illicit proceeds. Through this process the criminal tries to transform the monetary proceeds derived from illicit activities into funds with an apparently legal source.

In other words, money laundering involves disguising financial assets so they can be used without detection of the illegal activity that produced them. Through money laundering, the criminal transforms the monetary proceeds derived from criminal activity into funds with an apparently legal source.

Reasons for Combatting Money Laundering²

Money laundering is organized crime's way of trying to disprove the adage that "crime doesn't pay." It is an attempt to assure drug dealers, illegal arms dealers, corrupt public officials and other criminals that they can hide their profits and to provide them the fuel to operate and expand their criminal enterprises. Fighting money launderers and strengthening anti-money laundering efforts globally will reduce financial crime by depriving criminals of the means to commit other serious crimes. To a lesser extent, strengthening anti-money laundering regimes, particularly in the areas of identifying the originators of international wire transfers, will impact terrorist financing as well. At a minimum, strong anti-money launder-

ing measures help to create a body of evidence that exposes criminal behavior and help law enforcement identify violators and build cases against them that lead to their arrests, convictions and seizures of their assets.

Modern financial systems permit criminals to transfer millions of dollars instantly, using personal computers and satellite dishes. Money is laundered through currency exchange houses, stock brokerage houses, gold dealers, casinos, automobile dealerships, insurance companies, and trading companies. Private banking facilities, offshore banking, shell corporations, free trade zones, wire systems, and trade financing all have the ability to mask illegal activities. In so doing, criminals manipulate financial systems throughout the world. This process has devastating social consequences. For one thing, money laundering provides the fuel for drug dealers, terrorists, arms dealers, and other criminals to operate and expand their criminal enterprises. Furthermore, criminals manipulate worldwide financial systems to further a wide range of illicit activities.

Nations around the world are also victims of tax evasion schemes that use various financial centers and their bank secrecy laws to hide money from tax authorities, undermining legitimate tax collection. Financial centers that have strong bank secrecy laws and weak corporate formation regulations, and that do not cooperate in tax inquiries from foreign governments, are found worldwide. These financial

²Ibid.

centers, known as "tax havens," thrive in providing sanctuary for the deposit of monies from individuals and businesses that evade the payment of taxes in their home jurisdictions and allow them to keep the money they have deposited from the knowledge of tax authorities.

Unchecked money laundering can erode the integrity of a nation's financial institutions. Due to the high integration of capital markets, money laundering adversely affects currencies and interest rates as launderers reinvest funds where their schemes are less likely to be detected, rather than where rates of return are higher. Money launderers also negatively impact jurisdictions by reducing tax revenues through underground economies, competing unfairly with legitimate businesses, damaging financial systems, and disrupting economic development. Ultimately, laundered money flows into global financial systems where it can work to undermine national economies and currencies.

There is now worldwide recognition that we must deal firmly and effectively with increasingly elusive, well-financed and technologically adept criminals and terrorists who are determined to use every means available to subvert the financial systems that are the cornerstone of legitimate international commerce. The continued abuse of some offshore financial centers, the proliferation of online Internet banking and the widespread use of underground banks and moneychangers highlight

the importance of using new technologies and strong strategies to combat money laundering and terrorist financing schemes.

INTERNATIONAL TERRORISM FINANCING³

Terrorist groups differ from other criminal networks in the motive behind their crimes. While drug traffickers and organized crime groups primarily seek monetary gain, terrorist groups usually seek non-financial goals, such as publicity and political influence. Terrorism is a means to these ends. Terrorist financing also differs from money laundering in other respects. Ordinarily, criminal activity produces the funds and other proceeds that money launderers disguise so that the funds can be used for legitimate or criminal purposes. Funds that support terrorist activity are generated primarily through fundraising — often through legal non-profit entities, although terrorist groups often obtain funds from criminal activities as well. Because terrorist activity requires very little money (the attacks on the World Trade Center and the Pentagon are estimated to have cost a little more than half a million dollars), the amount of money that individual terrorist cells or their members seek to disguise is substantially less compared

³International Narcotics Control Strategy Report March 2001, "Money Laundering and Financial Crimes", <http://www.state.gov/g/inl/rls/nrcpt/2001/rpl/>

to that laundered by organized crime and drug kingpins. And it is the latter for which anti-money laundering tools were initially created. The investigation of terrorist financing is requiring law enforcement and regulatory officials to use existing anti-money laundering laws in altogether new ways. And it will require stronger international anti-money laundering enforcement regimes.

Small Sums With Big Effects

While they do not seek financial gain as a sole end, international terrorist groups need money to attract adherents and to support their activities. Some terrorist organizations also need funds for media campaigns, to buy political influence, and to undertake social projects aimed at maintaining membership and attracting sympathetic supporters. Often, terrorists also rely in part on funds gained from traditional crime such as robbery, kidnapping for ransom, drug trafficking, extortion, document forgery, currency and merchandise counterfeiting, and smuggling. Terrorists can then divert some of the proceeds of these criminal activities to their terrorist efforts.

A substantial portion of the terrorists' funding comes from contributors to nonprofit organizations, some of who know the intended purpose of their contribution and some of whom do not. In this key respect, terrorism financing contrasts with the financing of a drug trafficking network, which obtains virtually all of its funding from illegal activities.

Origins of Financial Support⁴

Terrorist groups commingle illicit revenues with legitimate funds drawn from profits from commercial enterprises and donations from witting and unwitting sympathizers. They tap a range of sources for their financial support including:

- *Otherwise Legitimate Commercial Enterprises:* Terrorist groups earn profits from businesses they own. They also secure donations from sympathetic entrepreneurs.
- *Social and Religious Organizations:* Since the early 1990s, terrorist groups have relied increasingly on donations from social and religious organizations for financial support.
- *State Sponsors:* Several rogue nations—Cuba, Iran, Iraq, Libya, North Korea, Sudan, and Syria— have provided material assistance, financial support or other resources to terrorists.

Moving Terrorist Money

Tracking terrorist financial transactions is more difficult than following the money trails of mainstream criminal groups. While many organized crime groups are adept at concealing their wealth and cash flows for long periods of time, their involvement in the phy-

⁴International Narcotics Control Strategy Report March 2001, "Money Laundering and Financial Crimes", <http://www.state.gov/g/inl/rls/nrcpt/2001/rpt/>

sical trade of illicit drugs, arms, and other commodities often exposes the revenues and expenditures connected to these illegal dealings. In contrast, terrorist actions generally are comparatively inexpensive and their financing is often overshadowed by the larger financial resources allocated for the group's political and social activities, making it more difficult to uncover the illicit nexus.

Terrorist groups use a variety of means to move their funds, including:

- *Currency Transport:* Cash couriered by operatives is difficult to track because there is no paper trail.
- *Traditional Financial Institutions:* The international nature of most foreign terrorist groups forces them to rely on banks and other financial institutions.
- *Islamic Banks:* Banks that operate in line with Islamic law, which prohibits the payment of interest and certain other activities, have proliferated throughout Africa, Asia and the Middle East since the mid-1970s. In most instances, these banks simply are not required to adhere to a wide range of regulations normally imposed on commercial banks. Islamic banks are often not subject to any regulatory and supervisory scrutiny by bank regulators, and thus, do not undergo periodic bank examinations or inspections. While these banks may voluntarily comply with banking regulations and in particular, anti-

money laundering guidelines, there is often no control mechanism to ensure such compliance. Some of the largest Islamic financial institutions now operate investment houses in Europe and elsewhere.

- *Money Changers:* Moneychangers play a major role in transferring funds in Asia, the Americas the Middle East, and other regions. Their presence is largest in countries where cash is an accepted means to finalize business deals and where large numbers of expatriates, work to remit funds to family abroad.
- *Underground Bankers:* Commonly referred to as alternative remittance systems, such as the Hawala or Hundi, underground bankers are prevalent throughout Asia and the Middle East.

FINANCIAL ACTION TASK FORCE (FATF) ON MONEY LAUNDERING⁵

The Financial Action Task Force (FATF) on Money Laundering is an intergovernmental body whose purpose is the development and promotion of policies to combat money laundering — the processing of criminal proceeds in order to disguise their illegal origin. These policies aim to prevent such proceeds from being utilized in future criminal activities and from affecting legitimate economic activities.

⁵FATF Web page, <http://www1.oecd.org/fatf/>

In addition to developing anti-money laundering measures the FATF encourages jurisdictions to adopt money laundering controls through the passage of legislation and policies designed to not only prevent proceeds of crime from being used to further criminal activities, but to facilitate the detection, investigation and prosecution of money laundering and terrorism on an international basis.

Member of FATF

The FATF currently consists of 29 countries⁶ and two international organizations, the European Commission and the Gulf Cooperation Council. Its membership includes the major financial center countries of Europe, North and South America, and Asia. It is a multi-disciplinary body — as is essential in dealing with money laundering — bringing together the policy-making power of legal, financial and law enforcement experts.

FATF Forty Recommendations⁷

This need to cover all relevant aspects of the fight against money

laundering is reflected in the scope of the *Forty FATF Recommendations* — the measures that the Task Force has agreed to implement and which all countries are encouraged to adopt. The Recommendations were originally drawn up in 1990. In 1996, the Forty Recommendations were revised to take into account the experience gained over the previous six years and to reflect the changes, which have occurred in the money-laundering problem.

Additionally, FATF has developed and published a series of interpretative notes that expand and further clarify the 40 Recommendations. Annually, the FATF also publishes a Topology Report that provides information on money laundering schemes and trends identified by member countries.

Subsequent to the terrorist attacks in the United States, FATF issued *eight additional recommendations* which, when combined with the FATF Forty Recommendations on money laundering, set out the basic framework to detect, prevent and suppress the financing of terrorism and terrorist acts.⁸

Summary of Forty Recommendations

The Forty Recommendations set out the basic framework for anti-money laundering efforts and they are designed to be of universal application. They cover the criminal justice system and law enforcement, the financial system and its regulation, and interna-

⁶The twenty-nine FATF member countries and governments are: Argentina; Australia; Austria; Belgium; Canada; Denmark; Finland; Germany; Greece; Hong Kong; China; Iceland; Ireland; Italy; Japan; Luxembourg; Mexico; the Kingdom of the Netherlands; New Zealand; Norway; Portugal; Singapore; Spain; Sweden; Switzerland; Turkey; the United Kingdom; and the United States.

⁷Available at Web page FATF Web page, <http://www1.oecd.org/fatf/>

⁸*Ibid.*

tional co-operation. It was recognized from the outset of the FATF that countries have diverse legal and financial systems and so all cannot take identical measures. The Recommendations are therefore the principles for action in this field, for countries to implement according to their particular circumstances and constitutional frameworks allowing countries a measure of flexibility rather than prescribing every detail. The measures are not particularly complex or difficult, provided there is the political will to act. Nor do they compromise the freedom to engage in legitimate transactions or threaten economic development.

The Recommendations are grouped into the following broad categories:

A. *General Framework of the Recommendations*

- Each country should take immediate steps to ratify and implement the Vienna Convention.
- A country's financial secrecy laws should not prohibit or impede the implementation of the Recommendations.
- There should be multilateral co-operation and mutual legal assistance and extradition in money laundering investigations and prosecutions.

B. *Role of National Legal Systems in Combating Money Laundering*

- Money laundering should be criminalized and expanded from

narcotics to all serious crimes generating substantial proceeds.

- Legal entities as well as individuals should be subject to criminal liability.
- Measures should be instituted to provide for the confiscation of property laundered, proceeds from and instrumentalities used or intended to be used in the commission of a money laundering offense.

C. *Role of Financial System in Combating Money Laundering*

- FATF Recommendations should apply to bank and non-bank institutions such as bureaux of exchange and to financial activities of non-financial businesses engaged in commercial activities.
- Strong customer identification and record keeping rules should be adopted.
- Steps should be undertaken to verify or determine a customer's true identity or on whose behalf transactions are conducted.
- Records of transactions should be maintained for at least five years.
- No anonymous or fictitious accounts should be maintained.
- There should be increased diligence of financial institutions for unusual large or suspicious transactions and prompt reporting to authorities as warranted.

- Financial institutions, their directors, officers and employees should have a safe harbor for disclosing information to authorities as required by law or regulation.
- Financial institutions should develop programs against money laundering that include policies, procedures and controls, ongoing training of employees and an audit function to test the system or program.
- FATF Recommendations should apply to the extent possible to branches of financial institutions abroad. Where this is not possible, special attention should be paid to transactions conducted in these branches to identify suspicious or questionable transactions.
- Cross border monitoring of cash and bearer negotiable instruments should be implemented.
- A central depository for currency and suspicious reports should be created.
- Bank and non-bank supervisory organizations should ensure financial institutions have counter-money laundering programs in place.

D. Strengthening of International Cooperation

- Information concerning international flows of cash should be recorded and shared so that estimated flows and reflows can be made from sources abroad.
- Information concerning trends and techniques should be disseminated.

- Suspicious transaction information should be shared "upon request".
- International cooperation should be supported by bilateral and multi-lateral treaties and agreements to facilitate detection, investigation, prosecution, extradition of defendants and the seizure or confiscation of property involved in or traceable to money laundering.

Summary of the Terrorist Financing Recommendations

At a Plenary Session on the Financing of Terrorism in Washington, D.C. on October 29th and 30th the FATF expanded its mission beyond money laundering. It now focuses its energy and expertise on the worldwide effort to combat terrorist financing. FATF issued new international standards to combat terrorist financing with the goal of denying terrorists and their supporters' access to the international financial system.

These recommendations require immediate steps to ratify and implement all relevant United Nations instruments, criminalize the financing of terrorism, terrorist acts and organizations, freeze and confiscate terrorists' assets, report suspicious financial transactions linked to terrorism, cooperate with and assist other countries in the fight against terrorism, regulate alternative remittance systems, impose stronger customer identifications standards, and ensure that nonprofit and other entities can not be used to support terrorist activity.

The FATF will require member countries to be in compliance with the new regulations by June 2002 and have action plans addressing those recommendations not already in place.

INDONESIA - THE NEXT PHASE

Recommendation 1: Financial Intelligence Unit

Indonesian law provides for the creation of a Center for Financial Reporting and Analysis (PPATK). This center or Financial Intelligence Unit (FIU) can be the linchpin of money laundering enforcement and regulation by becoming the central depository of currency and suspicious transaction reports, coordinating law enforcement and regulatory efforts at the national and international level, providing financial analysis and investigative training, and providing guidance and training to financial institution regulators and employees in the law and suspicious transaction reporting.

One problem is the recently passed Indonesian law that establishes a reporting level for currency transactions at US\$50,000. This unusually high reporting threshold will obviously place critical importance on getting financial institutions to recognize and report suspicious transactions, especially where the transactions are less than US\$50,000, if any useful information is to be derived from the reporting requirements. Failure to place emphasis on suspicious reporting could result in significant currency trans-

actions and criminal activity going unreported. Most countries have reporting thresholds of US\$10,000.

The newly established FIU should become a member of the worldwide network of Financial Intelligence Units known as the Egmont Group. The Egmont Group⁹ provides training and technical assistance to countries around the globe in the development and operation of Financial Intelligence Units and the formulation and implementation of counter-money laundering strategies.

An FIU can best be described as a central office that receives disclosures of financial information, analyses or processes them in some way and then provides them to appropriate government, law enforcement and regulatory authorities in support of a national and international anti-money laundering effort. In 1996, there was less than a handful of FIUs in the world. Today there are 58 jurisdictions that comprise the Egmont FIUs from all over the world. The FIUs have developed a network that allows the rapid exchange of intelligence and case related information to combat money laundering as well as terrorist financing.

Named after the venue in Brussels where the first such meeting of FIUs was held in June 1995, the Egmont Group serves as an international network, fostering improved communication and inter-

⁹FINcen Web page, <http://www.ustreas.gov/fincen/>

action among FIUs in such areas as information sharing and training coordination. The goal of the Group is to provide a forum for FIUs around the world to improve support to their respective governments in the fight against financial crimes. This support includes expanding and systematizing the exchange of financial intelligence information; improving expertise and capabilities of personnel employed by such organizations, and fostering better and secure communication among FIUs through the application of technology.

Recommendation II: Enact or Strengthen Laws to Fight Terrorism

The current Indonesian law does not specifically criminalize the act of terrorism or supporting terrorists organizations. This should be high on the priority list for future legislative development. The passage of a strong money laundering law is a strong first step to combating serious crime. Laws criminalizing acts of terror and support for terrorist organizations must complement the money laundering law to prohibit the use of its financial systems by terrorist organizations. The international consensus to fight terrorist financing has never been stronger. The international community is equipping itself with increasingly more effective tools to prevent and respond to terrorist financing. The Group of Eight (G-8) nations, the United Nations, the European Union, the Financial Action Task Force (FATF) on Money Laundering, and the

Organization of American States have all sponsored conferences and crafted recommendations designed to produce enhanced cooperation and strengthened measures to combat terrorist financing.

As further evidence of international resolve, on 28 September 2001, the United Nations Security Council (UNSC) adopted Resolution 1373, which reaffirms earlier UN counter-terrorism resolutions and requires states to combat terrorism and the financing of terrorism.

Recommendation III: Develop a System of Laws to Govern the Confiscation and Use of Property Derived from Illegal Activity

The new money laundering law (Article 32) provides for freezing of assets reasonably known or suspected to be the proceeds of crime pursuant to a written order of an investigator, public prosecutor or judge. Article 32 requires the financial services provider to freeze the assets and to submit a statement to the ordering authority within one business day of the freezing.

This Article is unclear who is responsible for assets not under the control of the provider of financial services and whether or how they should be confiscated or protected to prevent the removal or placement of assets beyond law enforcement or the courts.

Furthermore, there is no authority in the law providing for how proceeds

from confiscated assets can be used or for proceeds from the disposal of these assets to be placed in a centralized fund to ensure proper accounting or sharing either among agencies or organizations within Indonesia or with foreign jurisdictions involved in joint investigations.

Recommendation IV: Train Enforcement Investigators and Regulators

Intense financial investigations are essential in order to beat criminals at their trade — whether it is narcotics trafficking, organized crime, money laundering, or bank fraud. Tracing the money will lead to the top of the criminal organization. But financial investigations are extremely complex and difficult to conduct. *First*, it takes many years of working in the financial industry to understand all its intricacies. *Second*, no single agency possesses a sufficiently broad or cross-jurisdictional focus and information base to track financial movements. *Finally*, the sheer size, variety, and pace of change of the financial sector make financial investigations even more difficult. The tools of the money launderer range from complex financial transactions, carried out through webs of wire transfers and networks of shell companies, to old-fashioned, if increasingly inventive, currency smuggling. As soon as law enforcement learns the intricacies of a new laundering technique and takes action to disrupt the activity, the launderers replace the scheme with yet another, more sophisticated method.

Training investigators and regulators is a continuing process to keep abreast of the latest money laundering trends and techniques. Assistance in this area is available from a number of countries and organizations and should be pursued rigorously.

One resource is the Law Enforcement Academy (ILEA) in Bangkok, Thailand, which was established in March 1999. The curriculum and structure of this Academy is similar to the one located in Budapest, except for the shorter duration of the core course and an added emphasis on narcotics matters. Participation is opened to members of the Association of South East Asian Nations and the PRC. Trainers from the United States, Thailand, Japan, Holland, Australia and Hong Kong provide instruction.

Recommendation V: Identify and Understand Alternative Money Remittance Systems

Alternative remittance systems are not regulated in the new law. These remittance systems, sometimes also referred to as informal value transfer systems (IVTS), are a family of monetary remittance systems that provide for the transfer of value outside of the regulated financial industry. These systems should be identified and their operations understood by regulators, law enforcement and in particular providers of financial services if they come in contact with these services.

These systems¹⁰ are known by a variety of names reflecting ethnic and national origins, predominantly South Asian and Chinese. They operate throughout the world, especially in countries with large expatriate populations from Africa and Asia. Included, among others, are such systems as *hawala* (India), *hundi* (Pakistan), *fei ch'ien* (China), *phoe kuan* (Thailand), *hui k'uan* (Mandarin Chinese), *ch'iao hui* (Mandarin Chinese) and *nging sing kek* (Cantonese Chinese). Most of these systems pre-date the emergence of modern banking and other financial institutions. The Colombian Black Market Peso Exchange can also be characterized as a form of alternative remittance system.

These systems provide mechanisms for the remittance of currency or other forms of monetary value—most commonly gold—without physical transportation or use of contemporary monetary instruments. These systems are used extensively as a means for expatriates, such as foreign laborers, to have funds delivered to families in the home country without contact with authorities on either the sending or receiving end. The systems rely on a pairing of brokers, one who orders a disbursement on behalf of a sender and another that makes the dis-

bursement to the receiver, followed at some point in time with a clearing process to settle account imbalances between the brokers. The systems operate on the basis of a trusted relationship established in the context of narrowly defined ethnic and national ties. Records are not typically kept about the identities of the transactors or details of the transactions.

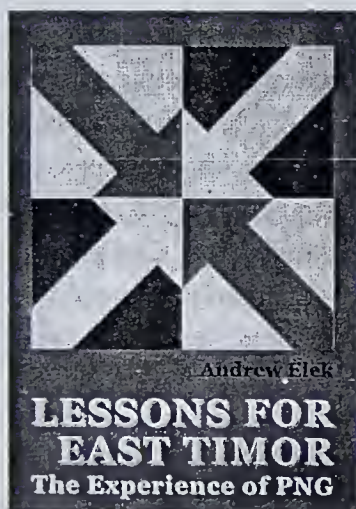
Because of the anonymity and secrecy of the remittance transactions, these systems are known to have been used in a variety of criminal activities including money laundering, terrorist financing, alien smuggling, drug trafficking, arms trafficking, corruption of government officials, currency controls evasion and tax evasion. Although these systems operate outside of the regulated financial industry, they may intersect with banks and other traditional financial institutions in order to either obtain currency needed to make disbursements, or as links in the account clearing process involving wire transfers, imports and exports of goods such as electronics, securities transactions etc. It is at these links that the brokers or their representatives may become known to financial institutions, and their transactions reviewed for indications of unusual activity that require the reporting of suspicious transactions. Again, the high currency threshold of US\$50,000 may allow banking transactions of these transmitters to go undetected unless they are identified and reported as suspicious transactions.

¹⁰International Narcotics Control Strategy Report March 2001, "Money Laundering and Financial Crimes", <http://www.state.gov/g/inl/rls/nrcpt/2001/rp/>

CONCLUSION

FATF anti-money laundering and terrorist financing recommendations are the foundation for implementing anti-money laundering and terrorist financing laws to provide a basis for eradicating or reducing serious crime and becoming a good international partner. Each country must not only continually assess and address its needs for law and policies to address problems unique to its culture and its legal and financial systems, but share information with countries throughout the world to minimize the financing of crime and terrorist activities.

Indonesia now faces a number of challenges. It must aggressively implement and enforce the new anti-money laundering statute, perform regular self-assessments to identify flaws and improvements to the law, and embark on an educational campaign to inform and educate the public, law enforcement, and the financial institution community of its requirements and benefits. The biggest challenge may be one of political will to stay the course and ensure that Indonesia does not provide a haven for criminal activity, which will certainly increase, if anti-money laundering and terrorist financing controls are not rigorously enforced.



LESSONS FOR EAST TIMOR The Experience of PNG

Written by Andrew Elek

Published by: CSIS, Jakarta

This publication, which was originally a paper presented at Dili Economic Policy Forum, was written by Dr. Andrew Elek who has worked extensively in development economics in the South Pacific as well as in South Asia. His deep understanding of the economic problems of Papua New Guinea (PNG) resulted from his experience as a senior official in the PNG Ministry of Finance from 1975-1979.

The author sees some similarities between PNG and East Timor; hence, some of PNG's experience is considered relevant to East Timor. There are some lessons to be

learned from PNG's success as well as from the mistakes it had made. This book presents sections that set out some features of the path trodden by PNG and its leaders since 1975. The implications for East Timor decision-makers are noted along the way.

This book consists of three sections. The first section, focusing on PNG's transition to independence, discusses PNG's constitutional and legal environment and open market. The second section examines PNG's deteriorating performance and crises in 1990s. Concluding remarks are presented in the third section.

This volume is very useful particularly for those who are interested in South Pacific as well as South Asian studies.

2002. 1st Ed., vi + 46 pp.; 25 cm, ISBN 979-8026-76-4, Rp 20.000,00.

Moluccan Influence on Dutch Foreign Policy

Robert Aspeslagh

INTRODUCTION

PEOPLE in diasporas¹ in particular living in a developed country, form a potential source of conflict in its country of origin.² Diaspora should be considered as a sub-category of transnationalism in which the political dimension is the overriding issue. In this paper the Moluccan people in the Netherlands are to be considered as a 'stateless diaspora',³ that can also pose a threat to the host country. Hence, Moluccans caused or suffered conflicts in both countries.

The conflict in the 1970s threatened the host country. In 1970, on the eve of a visit by the then President of Indonesia, Soeharto, to the Netherlands Moluccan youngsters occupied the residence of the Indonesian ambassador in Wassenaar. Some years later (1975) Moluccan youngsters laid siege to a passenger train at Wijster, whilst others occupied the Indonesian consulate in Amsterdam. In 1977 a second siege of a passenger train took place at the Punt (The Point) in conjunction with

the taking as hostages of pupils and teachers of a school in Bovensmilde. In 1978 the Moluccan youngsters burst in upon the Shire-Hall of Drenthe. With the exception of Wassenaar and Amsterdam, those events happened in the North of the Netherlands in the Province of Drenthe, where main concentrations of radical Moluccan youngsters could be found. At the turn of the Millennium the conflict in Indonesia took on the character of a civil war⁴ after an incident between a Christian bus driver and a Muslim passenger. In the years following that incident Muslim and Christian inhabitants of the Moluccas turned these islands into a battleground. They burned buildings and houses, destroyed villages, and chased their inhabitants away or killed them.

Both events caused a terrible shock in the Moluccan community in the Netherlands. Then, in order to achieve the Moluccan aim, i.e., independence through an independent state, the *Republik Maluku Selatan* (RMS),⁵ Moluccans attempted to obtain political influence⁶ over Dutch foreign policy

in Indonesia. Now the Moluccan community tried to push the Dutch Government to exert pressure on the Indonesian Government to restore law and order in the Moluccas. The characteristic of a modern diaspora community—a group with a clear ethnic identity preserved beyond generations, which is, through its societal participation, for example in education and labour, not tied to a homogeneous, low position⁷—could give possibilities and capabilities to influence the Dutch authorities and their policies towards Indonesia. Those attempts, however, encountered difficulties. In both states, Moluccans belong to rather small communities and these are divided into many sub-groups. Moreover, restrictions placed on a small democratic country vis-à-vis a large (un)democratic state, constituted a serious obstacle for the Moluccan community to exert influence. The downfall of a very repressive regime in Indonesia, however, presented new dimensions and capabilities to the Moluccan case.

Influence has to be distinguished from power. Small communities can have influence, if they can make an effective use of the public sphere.⁸ New generations of Moluccans in the Netherlands achieved other capabilities than their parents and grandparents. In exerting influence they also share new communication technologies.⁹ Furthermore, their parents and grandparents perceived the RMS as a political ideal which they collectively aimed at, whereas the new generations accept

the RMS at best as a symbol¹⁰ without being a practical objective. Moreover, the atrocities committed in the Moluccans after 1999 have changed the political climate in the Netherlands towards the Moluccan community; feelings of solidarity and sympathy arose.

THE MOLUCCAN ISSUE: 1970-1983

The occupation of the residence of the Indonesian Ambassador on 31 August 1970 by 33 young Moluccans marked an important moment for the Moluccan community in the Netherlands for its relationship with the Dutch Government. The then Moluccan leader, president of the RMS, Manusama, persuaded them to leave the residence, which they did. The immediate effect of their action was a delay of some days of the shortened visit of Indonesian's president Soeharto to the Netherlands. In October the Dutch prime minister and the minister of Foreign Affairs had a discussion with a small delegation. They discussed the opportunity of a dialogue with the Indonesian Government aiming at the possibility of Moluccans who wished to do so to return to their homeland and under what conditions. The Dutch Government expressed its willingness to mediate, but the diplomatic contacts with the Indonesian Government did not result into an acceptable agreement.

The tensions between the Moluccans and the Dutch Government, reinforced by feelings of powerlessness among the Moluccan community, frus-

trated in particular young Moluccans. They demanded strong actions against the Dutch Government, but their leadership was not prepared to do so, due to a long tradition of obedience to authority, not only as an effect of a colonial military¹¹ heritage, but also because of their cultural background,¹² and a deeply rooted Christian faith.¹³ Most of their radical actions against the Dutch Government were hatched in the municipalities of Assen and Bovensmilde, located in the North of the Netherlands. In these Moluccan neighborhoods plans were developed to lay siege to trains, to occupy the Indonesian consulate in Amsterdam and a school in Bovensmilde. These plans were carried out respectively on 2 December 1975 in Wijster and Amsterdam and on 23 May 1977 in the Punt and in Bovensmilde.

A strong argument favoring those actions was the speech of the then queen Juliana on the occasion of the independence of the Dutch colony of Surinam on 25 November 1975. In her speech, she stated that 'each people has the right to freedom.' Moluccans were asking themselves why this did not apply to them; however, the Dutch Government had made such a suggestion in the past. Another argument to develop their plans were the negotiations between the Indonesian and Dutch governments, which resulted in the so-called Wassenaar Agreement of 1974/75.¹⁴ The Agreement laid down the conditions, which made it possible for Moluccans to visit Indonesia as well

as improved the opportunity to return to Indonesia. In order to elaborate the Agreement, so called Joint Committees¹⁵ were installed both in the Hague (Netherlands) and Jakarta (Indonesia). In the Hague the Joint Committee consisted of representatives of the Indonesian Embassy, the Netherlands Ministry of Culture, Recreation and Social Work (CRM), and the Netherlands Ministry of Foreign Affairs.

CRM was the leading ministry with respect to the Moluccan issue and also the trustee of the Agreement. In a discussion of the Permanent Parliamentary Commission on Culture, Recreation and Social Work with the Deputy Minister of Foreign Affairs, the following conclusions were drawn.¹⁶ *First*, the Dutch Government takes for granted that the future of the majority of the Moluccans living in the Netherlands will be in this state. With respect to this issue the Dutch and Indonesian Governments have agreed to establish a Joint Committee of Dutch and Indonesians, which has to promote the dialogue between the Moluccans in the Netherlands and the Indonesian people and to exchange information.

Second, the Dutch Government considers the discussion about the Moluccan political aspirations as concluded. The Parliamentary Under-Secretary of Foreign Affairs stated that the Minister of Foreign Affairs has assured the Indonesian Government that the Dutch Government does not share the Moluccan aspiration for an in-

dependent South-Moluccan Republic (RMS). Nonetheless, the Dutch Government cannot prevent such striving, due to the constitutional freedom of expression of opinion.

On the other hand, the Indonesian Government recognized the difficulties of the Dutch Government with respect to the Moluccan population in the Netherlands. Therefore, the Indonesian Government promised among others: Although the Dutch Government is fully responsible for the Moluccans in the Netherlands, Indonesia is willing to support the Netherlands in resolving the problems with the Moluccan community.

Indonesia is willing to promote integration of the Moluccan people in the Netherlands, amongst others by allowing the Indonesian society to maintain contacts with the members of the Moluccan community in the Netherlands, also in those cases of Moluccans who are stateless.

The policy of the Dutch Government towards the Moluccan Community was crystal clear: 'The Government holds those contacts (with the Indonesian authorities, RA) of great value and it will promote them as much as possible, convinced that the acquaintance with the altering societal patterns in Indonesia could contribute to more openness with the Moluccans for the Dutch society. (...) These contacts also create the capability to test the quality of the reality of the future ideals which are fostered in the Moluccan

Community.'¹⁷ These premises with respect to the wishes and actions of the Moluccan Community ran like a continuous thread through the Dutch Moluccan and Indonesian policies for the forthcoming decades. In other words, 'Contacts with the Moluccas and non-recognition of the RMS were besides integration with the maintenance of the own identity the corner stones of the administration.'¹⁸

The Joint Committee contributed in two ways to the issue of the Moluccans in the Netherlands. *First*, the central idea that visits to the Moluccas had to have a sobering effect on the perceptions of the future of Dutch Moluccans in the Moluccas was implemented through the organization of so called orientation journeys.¹⁹ *Second*, the history of the Moluccan Community was regarded full with myths.²⁰ A first historical research in order to achieve a history more in accordance with truth an official of the Netherlands Ministry of Foreign Affairs made an investigation into the past and the causes of the Moluccan diaspora.²¹ In 1977 the *Commissie van Overleg Zuid-Molukkers-Nederlanders* (Commission of Consultation South-Moluccans-Dutchmen) also known as the Commission Köbben-Mantouw assigned a researcher to write an historical survey about the Dutch-Moluccan past. In 1978 the Commission Köbben-Mantouw issued a Report.²² The Report consisted of four parts — three sections and one introductory chapter. Its aim was to find an answer

to questions, which exist in the Moluccan Community.

The results of the deliberations of the Joint Committees, however, were disappointing for the Moluccan Community in the Netherlands, in particular because the Dutch Government rejected the cry for an independent state. Out of many protests one example. The political organization of the RMS, the *Badan Persatuan*, wrote to the Dutch Prime-Minister that the 'Executive Council of the *Badan Persatuan* means well to send You an announcement, in which it has embodied its point of view *vis-à-vis* the results of the discussions —about us, however without us— at the end of November 1981 in Jakarta between the Dutch and Indonesian delegation in the framework of the Agreements of Wassenaar. Decisions about us without us are not only grievous, but they can lead to tensions and disappointments, which are not conducive to a good understanding between the Dutch Government and the South Moluccans in this country.'²³

Although the Moluccan leadership as well as the actions of Moluccan youngsters had had influence on the Dutch foreign policy towards Indonesia, the effect was not what they had hoped, but the opposite of it. Hence, they sought for their own influence on foreign policies. Amongst others the following events occurred:²⁴

- In 1971 via the chairman of the Indian United Nation Association (UNA), a Non-Governmental Organ-

ization and member of the World Federation of United Nations Associations (WFUNA), a delegation of Moluccan youngsters attended a WFUNA meeting in Geneva. The delegation addressed the Moluccan case to one of the commissions. In their declaration they stated that they were prepared to negotiate with the Indonesian Government without conditions laid down beforehand. Nine delegations supported the Moluccan declaration;

- On 29 September 1976 the independent republic of Benin pleaded at the general Assembly of the United Nations for the independence of the South-Moluccas. This country had recognized the RMS, however, not the leaders behind Manusama, but his opponent in the RMS, Tamaela. Although Tamaela was a solitary acting person, he reinforced the RMS — ideal amongst the Moluccan youngsters and he aroused dissatisfaction with the policy of Manusama;
- In 1976 representatives of the Manusama group in the RMS visited Paris for contacts with a Vietnam delegation, which negotiated with the United States to terminate the war in Vietnam. In particular the young Moluccans were very positive about these contacts, because their political attitude was not against socialist or communist regimes;
- On 22 November 1980 a Note of Protest was mailed to the Confer-

ence on Security and Co-operation in Europe, in which attention was requested for the 'intolerable position of the South Moluccan refugees in the Netherlands.' In this Note a special Committee of Investigation was demanded 'in order to closely inquire into the whole matter and to make a thorough study of the policy, the Dutch Government has been pursuing towards the South Moluccan refugees, since their compulsory transport to the Netherlands in 1951.'²⁵ Despite this attempt the Moluccan representatives did not succeed to get into the CSCE in Madrid;

- In November 1982 the president of the RMS, J. Alvarez Manusama, addressed the Fourth Committee of the United Nations General Assembly about East Timor. In this Address Manusama suggested to the Fourth Committee 'to consider relevant steps towards the reopening of the question of decolonisation of Indonesia.'²⁶ He also compared the Indonesian regime with Hitler²⁷ and he accused Jakarta of conducting an imperialistic expansionist policy.

The RMS recognized that it had failed to reach its aims through the Dutch Government as well as through international contacts. Also a Member of Parliament of the Christian Democratic Appeal (CDA) —the then biggest party and part of the Government— who in 1978 visited the Moluccas, expressed the opinion that

the RMS had no *raison d'être*.²⁸ In that same year the *Commissie van Overleg Zuid-Molukkers-Nederlanders* (Commission of Consultation South-Moluccans—Dutchmen), which was established due to the unrest among the Moluccan Community, issued a Report about the Round-Table Conference on the Independence of Indonesia. In this Report the Commission stated that 'on the one hand the South-Moluccans have to acknowledge that at the time the Dutch Government did its utmost to achieve the right on self-determination. On the other hand the Commission is of the opinion, that the Dutch Government and the Dutch people have to understand and to admit that even now the striving for self-determination of the South-Moluccans is also fuelled by what has been advocated by the Dutch Government in her fight for self-determination of several territories of Indonesia.'²⁹

Although it was acknowledged that both sides had contributed to the present situation of the Moluccans in the Netherlands, in 1980 Manusama stated after a visit of the Dutch Prime-Minister to Indonesia, that 'again this (Dutch) Government underscores the position, that it is not willing to co-operate in a positive way in the solution of our problems. How much goodwill Van Agt (the then Prime-Minister, RA) could have achieved if he had visited the Moluccas in person.' He considered the relationship between the RMS and the Dutch Government worsened since the Governmental Policy

Paper of 1978, in which the right to self-determination of the Moluccan people was completely neglected.³⁰ The conclusion that Dutch policy towards the Moluccan people in the Netherlands had failed was almost general.³¹ The Wassenaar Agreement did not fulfil the wishes and aims of the Moluccan Community in the Netherlands. The enforcement of the Agreement gave rise to conflicts among and with the Moluccans, who took part in the visits. The ideal of the independence had not come closer.³²

The impact of the actions of Moluccan youngsters was considerable. They achieved much, but not directly through the foreign policy of the Netherlands. Since both the Netherlands and Indonesia regarded the Moluccan issue a Dutch internal problem, the Netherlands treated them as a national and social-cultural matter. The leading ministry became CRM aided by the Deputy Minister of Foreign Affairs during the negotiations with the Indonesian Government. It also became clear that the RMS had lost its *raison d'être* and therefore, could not play a significant role in influencing Dutch foreign policy in Indonesia.

THE MOLUCCAN ISSUE: 1999-2002

A second wave of violence, which shocked the Dutch Moluccan Community, did not occur in the Netherlands but in Indonesia. A minor incident on the 19th of January 1999 caused a chain-

reaction of violent atrocities in the Moluccas,³³ which upset and concerned the Moluccans in the Netherlands, who still have many family ties in the Moluccas. The deep roots of the conflict may date back to the colonial time. The roots of the present conflict, however, have to be ascribed mainly to fifty years of Indonesian rule, in particular of the Soeharto regime.³⁴ The conflict and its accompanying atrocities are an Indonesian problem, which have to be solved by the Indonesian Government. The incompetence³⁵ of the Indonesian Government to resolve the conflict and to establish order and peace in the region, however, worsened the conflict. The Dutch Government, facing a Moluccan Community in despair about the atrocities in the Moluccas, had to act. The delicate relationship between Indonesia and the Netherlands, due to a long common history of colonialism and the Dutch reluctance to accept a Unitarian Indonesian state, induced the Netherlands to seek for a multilateral approach to push the Indonesian Government to take actions in order to restore peace and security in the region.

In December 1998, at the instigation of the Dutch Ministry of Foreign Affairs, a delegation of the European Union visiting Jakarta expressed to the then president of Indonesia Habibie its serious concerns about religious violence in Indonesia. In January 1999 the Dutch again requested the European Union to impress upon the Indonesian

Authorities the need to restore peace and security in the Moluccas. The European Union pressed the Indonesian Government in July 1999 again to restore peace and security in the Moluccas. May 2000, on the initiative of the Dutch Government, the European Union expressed its deep concerns about the developments in the Moluccas.

The European Union intervened, after a request of the Dutch Government, with the Indonesian Authorities in order to take steps against the Laskar Jihad warriors. In October 2000 a delegation of the European Union headed by the French Ambassador, which consisted of representatives of embassies of 9 member states —Belgium, Germany, France, Greece, Italy, Netherlands, Portugal, Sweden and the United Kingdom— visited the Moluccas. In the Report³⁶ the European Union admitted that the conflict is an internal Indonesian problem, which has to be resolved by the parties involved. In this respect the European Union will support the Indonesian territorial integrity. The European Union, however, stressed her concerns about the tensions and violence in the Moluccas, because they prevent the pursuit of the population's fundamental rights. Also in October 2000 the European Union issued a statement in which it demanded attention for the situation in the Moluccas.³⁷

A second mission of the European Union to the Moluccas headed by the Swedes took place from 20-22 February

2001.³⁸ The then Swedish EU-Presidency and the Commission concluded that, due to the economical background of the conflict, first priority should be given to the economical development of the region. Moreover the European Union was prepared to give permanent humanitarian aid, but each program for the Moluccas had to be devoted to the process of reconciliation and reconstruction. In order to understand the problems raised by the process of decentralisation of government the European Union was willing to offer to the Indonesian Government its assistance in the identification, elaboration and implementation of practical conflict prevention and resolution measures.³⁹

The Dutch Government perceived the European Union as the main multi-lateral platform to internationalise the issue of the Moluccas, but it also approached other international governmental organizations to pursue the issue of the Moluccan conflict and to urge Indonesia to take the necessary steps to restore peace and security. Its main focus in this respect consisted of providing emergency aid through the UNDP.⁴⁰ Although the Netherlands, in that period were both member and chairman of the UN Security Council, they were not in the position to internationalise the conflict in this body.⁴¹ During the sessions of the Security Council of the United Nations in July 2000, the United States, France and the Netherlands raised the issue

of the Moluccas.⁴² In an appeal the United States urged Indonesia to restore order in the Moluccas and to provide the necessary basic needs to the stricken communities. Despite the attempts of the Netherlands to request more attention for the situation in Indonesia, in particular in the Moluccas, no resolution regarding the situation was adopted.⁴³ Also the ASEAN was approached by the United States on the request of the Dutch Government to put pressure on the Indonesian Government.⁴⁴

This brief overview of the diplomatic and aid steps of the Dutch Government to internationalise the conflict in the Moluccas, indicates that it wished for the support of the European Union and the larger international community in order to put pressure on the Indonesian Government to settle the conflict. However, the Dutch Government, in particular the Minister of Foreign Affairs,⁴⁵ also took direct steps towards the Indonesian Government. In March 1999 the Dutch Minister of Foreign Affairs discussed the matter with his Indonesian colleague. One month later the Dutch Ambassador in Indonesia visited the Moluccas and consulted with the regional and military authorities. The bilateral co-operation both through the Ministries of Foreign Affairs and the Development Co-operation were intensified after Abdurrahman Wahid was installed as the President of the Republik Indonesia. Despite attempts of the Dutch Minister of Foreign

Affairs to take diplomatic steps towards the EU, the United States and the Asian partners in order to restore peace and order in the Moluccas, the Dutch Government maintained her position that Indonesia had the duty to solve the problem. How delicate the Dutch position was became clear by a letter⁴⁶ of the Dutch Minister of Foreign Affairs to his Indonesian colleague. In this letter he offered assistance to the Indonesian Authorities in order to contribute to the restoration of peace and reconciliation.

In particular his remark that in a situation in which trust between the parties had disappeared a neutral attitude of the Indonesian police and army was essential caused a rather negative response both in the Netherlands and Indonesia. Indonesia perceived the Moluccan conflict as an internal problem and did not accept foreign interference. Suggestions to allow humanitarian intervention by foreign countries was strongly rejected by the Indonesian Government.⁴⁷ Despite this attitude with the consent of the Indonesian Government, the Netherlands Ministry of Foreign Affairs supported among others the professionalisation and democratisation of the Indonesian military financing a workshop 'Conflict Resolution' in Jakarta, that was attended by MP's and the military.⁴⁸ Also initiatives of Moluccans in the Netherlands to meet with their counterparts in Indonesia received assistance of the Ministry of Foreign Affairs.⁴⁹

INTERACTIONS BETWEEN THE DUTCH AUTHORITIES AND THE MOLUCCAN COMMUNITY

With the events of the 1970s in mind, the Dutch Government was on the one hand rather concerned about the reaction and possible actions of Moluccans in the Netherlands due to the cropping up of tension within the Dutch Moluccan Community. Hence it could happen that the Moluccans would act as a people in diaspora and try to intervene in the Moluccas, which would fuel the violence in that region as well as disturb the friendly relationship with the Indonesian authorities, in particular with the then in the Netherlands very popular president Wahid. As a consequence an interaction occurred between the events in the Moluccas and the Dutch Government.⁵⁰ However, a repetition of the violent events of the 1970s could occur in the Netherlands. In particular two ministries became very active: the Ministry of Foreign Affairs and the Ministry of Home Affairs, especially its Minister for Big Cities and Integration Policy.⁵¹ The Dutch Government was very much aware that the Moluccan Community in the Netherlands watched the developments in the Moluccas with great concerns. It understood their feelings of anxiety about the well being of their relatives and acquaintances in the Moluccas as well as their feelings of powerlessness.⁵² The Minister of Big Cities and Integration Policy was the coordinating ministry for the contacts

between the Moluccan Community and the Dutch Government. The Minister regularly consulted with Moluccan political, ecclesiastical, societal and aid organizations in order to inform them about Dutch policy towards Indonesia. Other objectives of the Dutch Government were:⁵³

- To keep itself informed on the developments within the Moluccan Community;
- To contribute to the coordination of assistance to the Moluccas by Moluccans in the Netherlands;
- To promote communication between the various Moluccan religious communities;
- To avert the transfer of the conflict in the Moluccas to the Dutch Moluccan Community.⁵⁴

The situation in the Moluccas prevented the Joint Committee to carry out its regular tasks.⁵⁵ Hence the Committee made 1 million Dutch guilders available to the Indonesian minister of Combating Poverty and Social Welfare to be employed in reconstruction and utility projects of Moluccan NGOs. Moreover it was decided that on 31 December 2002 the present engagement for repatriation would be terminated, although after 2002 individual cases could return to Indonesia under the same conditions.

The civil war in the Moluccas, however, provoked the more radical Moluccans in the Netherlands to take action. A threatening call to make an attempt

on the life of the Queen, shortly before the National Remembrance Day of those killed in World War II on the 4th of May 2000, compelled the Dutch Government to take strong security measures. The Prime Minister, however, immediately warned the public not to put the blame on the Moluccan Community.⁵⁶ In particular the *Vrije Molukse Jongeren* (Free Moluccan Youth) severely criticised the Government. They threatened to take violent actions with molotov cocktails and bombs, first without victims. If intervention in Indonesia did not take place the actions would become tougher against the Dutch society. Targets could be the Minister of Foreign Affairs or the Prime Minister.⁵⁷ Other organizations of Moluccans, People Against Genocide (PAG) and Maluku Warchild,⁵⁸ also announced tough actions against the Dutch society. However, the violent actions in the Netherlands were small in number and they caused relatively little damage. But they did have a negative effect on the image of the Moluccan Community.

The RMS appeared in the limelight when a letter of its President, Tutuhaturunewa, was leaked to the broadcasting organization VARA. In this letter Tutuhaturunewa wrote that the RMS Government in exile had sent money to armed resistance groups in the Moluccas.⁵⁹ Two former members of the RMS-Government, who had resigned due to internal disagreements with the policy of Tutuhaturunewa, criticised this action of the RMS. The whole affair

caused some articles to be published in the newspapers, but soon lost its newsworthiness. However, this action as well as a declaration, both in Ambon and the Netherlands, of the *Front Kedaulatan Maluku* (Sovereignty Front of the Moluccas/FKM), that the South Moluccas have the right of self-determination, did not cause many problems in the Netherlands. But they served the adversaries of the Christian Community in the Moluccas. In the Moluccas the RMS became again the synonym for Christian and thus the bugaboo of the conflict, that had to be opposed, preferably with the use of violence.

On the part of the Dutch Government as well as provincial and local authorities initiatives were started to make contacts with representatives of the Moluccan Community. The first invitation to hold talks between the Dutch Government and the Moluccan Community on Monday 18 September 2000, however, was not accepted by various Moluccan groups. The RMS refused to take part in the meeting, because in its opinion the Government did not take the RMS-Cabinet in exile serious. The six Moluccan Protestant Churches were of the opinion that the importance of the talks with the Dutch Government had diminished, because the Government was more concerned with the threats of attacks by Moluccan youngsters⁶⁰ and not with the shocking situation in the Moluccas. Moreover they held the view that only one hour for the talks

was not a very respectful gesture to the Moluccans. Notwithstanding the objections of Moluccan representatives, at a meeting of the Government⁶¹ with five Moluccan organizations on 17 October 2000 it was agreed, that they would meet two to three times a year in order to keep the Moluccans informed about the efforts of the Government against violence in the Moluccas. Not all the Moluccan participants were satisfied with the result of the talk. Although the RMS had the impression that the Dutch Government did its best, it was not satisfied with the efforts. The representative of the Free Moluccan Youth was dissatisfied and also of the opinion that the Netherlands could have done more.⁶²

Furthermore, the Minister for Big Cities and Integration Policy held among others talks with Moluccan youngsters. The first formal discussion took place on 20 February 2001. Most of the Moluccan youngsters present at the meeting were of the opinion that the meeting had been successful, but the Free Moluccan Youth said that they would not attend another meeting, whilst the RMS-youth had some reservations about attending another one.⁶³ A group of Moluccan youngsters, who did not want to represent one particular organization or group, decided that they would continue to attend the talks and to develop a programme with young Moluccans in Indonesia.⁶⁴

CONCLUSIONS

The atrocities in the Moluccas around the turn of the Millennium caused intensive contacts between the Moluccan Community and the Dutch Government. The policy of the Dutch Government 'to keep itself informed of the developments within the Moluccan Community' and 'to prevent the conflicts in the Moluccas from spreading to the Dutch Moluccan Community' has been successful. The results of these contacts indicated that due to a policy of establishing Moluccan organizations⁶⁵ after the violent actions in the 1970s, tensions within and with minority communities did not have a significant affect on policy choices. Institutional arrangements had overcome the negative implications of the tensions with and within the Moluccan Community.⁶⁶ Both foreign policy and home policy regarding the Moluccan Community in the Netherlands went hand in hand in order to avoid violent actions of Moluccans, in particular youngsters.

Since 1975 the actual aims of Dutch policy towards the Moluccan Community have not fundamentally changed. On the other hand, the Moluccan Community had profoundly altered, due to the coming up of new generations, who were born and raised in the Netherlands, and to the growing insight that their future is in the Netherlands. As a result, the RMS turned out to be a less than credible represent-

ative of the Moluccan Community to the Dutch Government contrary to what it had been in the Seventies. In the Seventies and Eighties it was able to exert influence on both the Dutch Government and the Moluccan Community. The position taken by the RMS during the civil war in the Moluccas and the reactions of the Moluccan Community in the Netherlands proved that it had not only lost its ideal of an independent Moluccan Republic, but almost also its function as a symbol for the Moluccan Community.⁶⁷ Threats of violence did find very little support within the Moluccan Community. Those threats were confined to a small group of mostly young activists or a single individual. The main stream of young Moluccans is not striving for an independent Moluccas, but wants to co-operate with the Dutch authorities in order to ease the fate of their Moluccan relatives and friends in Indonesia.

Many Moluccans in the Netherlands became active, due to the atrocities in the Moluccas. They started relief actions in order to support their families, acquaintances and villages in that region. Most of those actions were a reflection of the fragmentation in the Moluccan Community and therefore rather particularistic and small. Apart from this there is among others aid provided by the Foundation 'Help Ambon in Nood' (Help Ambon in Distress) in which both Moluccan Christians and Muslims are participating.

The violent actions of the Seventies have affected Dutch Foreign Policy towards Indonesia and, in general, the bilateral relations with Indonesia. The effect, however, was not what the Moluccans wished to achieve, an independent Moluccas, but aroused the awareness both in Indonesia and the Netherlands that the authorities had responsibilities with respect to the feelings of the Moluccan Community in the Netherlands. The Joint Committee has done its work. The Wassenaar Agreement of 1974/75 has been successful. Learning about the actual situation in the Moluccas through information, repatriation of a small number of Moluccans, and through new means of communication, Dutch Moluccans became aware that there was no future for themselves in the Moluccas, but that they could be helpful to their relatives, extended families, and villages of origin by providing some basic needs. Humanitarian assistance became more important than political action for an independent Moluccas. Ratio and emotion regarding the situation in the Moluccas and the future of the Moluccans both in the Netherlands and Indonesia were brought into equilibrium.

The events in the Seventies also influenced Dutch Foreign Policy towards Indonesia during the first years of this new Millennium. Although the Netherlands have a preference for solving issues along multilateral channels, bilateral contacts were actively used in order to convince the Indonesian Government that it should take

proper action to restore peace and security in the Moluccas. The Dutch Government was very aware of the feelings of the Dutch Moluccan Community and it wished to avoid new acts of violence. At first, the Dutch Government had hoped to deal with the atrocities in the Moluccas by quiet diplomacy. However, the strong Moluccan reaction and Moluccan requests to the Government to act, forced it to explain what actions had been undertaken.⁶⁸ Pressure on the Government by Moluccan leaders to push for humanitarian intervention were taken over at best half-heartedly, due to the opinion of the Government that the Moluccan issue was an internal Indonesian matter and knowing how sensitive the Indonesian Authorities are. In fact, the Moluccan Community did not exert direct influence on Dutch foreign policy, but it influenced the way the Dutch foreign policy was expressed.

The policy of the Dutch Government towards the Moluccan Community has had its positive effects. What in the Seventies could create a climate of violence within the Moluccan Community in the Netherlands was almost non-existent at the turn of the Millennium when the atrocities in the Moluccas began. After 25 years, violence against the Dutch or the Dutch society in order to involve the Dutch authorities in Moluccan matters was not a real option anymore. The RMS lost its meaning for the vast majority of Moluccans. Representatives of the Moluccan

Community and the Netherlands Government cooperated in order to prevent the transfer of the conflict in the Moluccas to the Netherlands as well as steps that could be taken by the Netherlands vis-à-vis Indonesia in order to make an end to the atrocities in the Moluccas. In other words, the Dutch authorities as well as the Moluccan Community in the Netherlands have left the shadows of the past behind.

Although drawing a parallel between two periods in the Dutch-Moluccan history seems to be a comparison between apples and pears. Both are, however, fruit and located in the same bowl. The events in the 1970s in the Netherlands and in the turn of the Millennium in Indonesia are clearly interlinked. The developments after 19 January 1999 in and between the Moluccan Community in the Netherlands and the Dutch Government have to be seen in the light of the 1970s. The traumatic events of the 1970s forced the Netherlands Government to act as active as possible within the existing frameworks of foreign policies. The Malino Agreement, concluded on 12 February 2002, is pinning hopes that the 3-year old civil war in the Moluccas will end, by furthering an agenda of security recovery, law enforcement, and rehabilitation of social economy.⁶⁹ The Agreement was negotiated after several years of, amongst others, foreign pressure on the Indonesian Government. In this process, the Netherlands Government played an active, but, due to its limited possibilities, restrained both multilateral and bilateral roles.

ENDNOTES

- 1 For Anthony Smith 'Diaspora' is a subordination of 'ethnic-nationalism'. 'Pre-independence' movements whose concept of the nation is basically ethnic and genealogical will seek to secede from a larger political unit (or secede and gather together in a designated ethnic homeland) and set up a new political "ethno-nation" in its place; these are secession and *Diaspora* nationalisms.' In: Smith Anthony D., *National Identity* (London: Penguin Books, 1991), 82. Gabriel Sheffer presents the following definition of modern ethno-national diasporas: these 'are social and political entities that arise from migration (which may be voluntary or imposed and is usually from an ethno-national state or homeland) to one or more host countries. Members of diaspora communities permanently reside in host countries, which distinguishes them from transient migrants, refugees and guest workers who only temporarily reside in host countries.' In Gabriel Sheffer, 'Ethno-National Diasporas and Security,' *Survival* 36, no. 1 (Spring, 1994): 61.
- 2 Paul Collier and Anke Hoeffler (4 January 2001), *Greed and Grievance in Civil War*. World Bank, Working Paper No.: 2355, 5. Both authors investigated causes of civil wars. Diasporas could increase the provision of finance of rebellion because: 'Diasporas are usually much richer than the population in their country of origin. They are better placed for collective action: emigrants have a cultural incentive to create diaspora organizations, which can then discipline free riding. They do not suffer the consequences of the conflict.'
- 3 Sheffer, 'Ethno-National ...,' 63.
- 4 Almost three years of sectarian fighting between Christians and Muslims has left more than 5,000 people dead (*The Jakarta Post*, 12 December 2001). With this data we can speak of a civil war if we take into a definition of civil war the killing in fights between the inhabitants of a region or country of at least 1000 people in a year.
- 5 The Republik Maluku Selatan was supported by mainly the Christian population in the Moluccas, but is now almost only defended by a minority among the Moluccan Community in the Netherlands.
- 6 Cox, Robert W. and Harold K. Jacobson (1973), *The Anatomy of Influence. Decision Making in International Organization* (New Haven and London: Yale University Press, 1973), 4. 'Influence is to be distinguished from power. Power means capability; it is the aggregate of political resources that are available to an actor. These resources may be material or not. Power may be converted into influence, but it is not necessarily so converted either at all or to its full extent. Although those who possess the greatest power may also exercise the greatest influence (...). Influence has specific scope: an actor influences another's behaviour in some particular sphere of activity, or issue-area. Some actors may have resources enabling them to exercise influence in many domains, but at any one time they may really concerned and willing to exercise it in only a few. An actor with relatively limited resources but greater intensity of concern may achieve greater influence in a particular area than another who has greater resources but less immediate concern. Intensity of interest may also explain why some actors are harder to influence than others who care less about the matter in question.'
- 7 Nonetheless the data of a survey on the participation in Dutch education of Moluccan children are not very promising: for example 85% of the Moluccan youth is advised to attend the lower vocational and general education (vbo/mavo); 22% is drop outs and about 50% takes a vbo/mavo-diploma. For the whole population in the Netherlands the percentage advised to attend lower vocational and general education is about 34%. See: Veenman, J. (2000), *Molukse jongeren in Nederland. Integratie met de remainder* (Moluccan Youth in the Netherlands. Integration with a Drag). Assen: Van Gorcum, 2000.
- 8 James Bohamn, "International regimes and democratic governance: political equality and influence in global institutions," *Foreign Affairs* 75, no. 3 (1999): 499-513. Quotation on p. 503. 'Access to political influence is then not merely a matter of opportunity, since "influence" here also means something like the effective use of free public reason. Being effective in the public sphere is not a matter of agency (of bringing about a specific outcome), but of having the reasonable expectation to be able to influence deliberation about decisions that affect one's lives. This is not a matter of having particular opportunities or resources (however important they may be), but of capability. Citizens must possess the capability for

adequate functioning; that is they must possess the capabilities necessary to make full and effective use of their public freedom, so that all citizens possess a minimum level of capability for public functioning.'

- 9 Michael Dahan and Gabriel Sheffer, "Groups and Distance Shrinking Communication Technologies," *Nationalism & Ethnic Politics*, 7, no. 1 (Spring, 2001): 85-107. See also: Fridus Steijlen, *Kerusuhan. Het misverstand over de Molukse onrust* (Kerusuhan. The misunderstanding of the Moluccan unrest). (Utrecht: Forum, 2001), 22-26.
- 10 See, F. Steijlen, *RMS: van ideaal tot symbool. Moluks nationalisme in Nederland 1951-1994* (From ideal to symbol. Moluccan nationalism in the Netherlands 1951-1994). (Amsterdam: Het Spinhuis, 1996).
- 11 In 1951 about 3500 Moluccan military with their families came to the Netherlands. They were soldiers, who served in the Dutch Colonial Army (KNIL).
- 12 In the Moluccan tradition and culture the authority of the oldest people was strong and youngsters had to obey.
- 13 In 1952 the Geredja Protestan Maluku (GPM - Moluccan Protestant Church) at Ambon issued a pulpit sermon in which the church stated, based on Rom 13, that Christians in the Moluccas had to obey Indonesian authority. The Protestant Moluccans in the Netherlands did not agree with the statement and they established the *Noodgemeente Geredja Protestan Maluku di Belanda* (NGPMB - Temporary Protestant Moluccan Church in the Netherlands).
- 14 The Wassenaar Agreement was not made public, but kept secret, on the request of the Indonesian Government, but seconded by the Dutch Government. Proceedings were instituted, with an appeal to the Law on Disclosure of Administration (WOB), against the Dutch Government to disclose the Agreement, but they were lost. The secrecy of the Agreement has probably a political background related to individual cases. There is a chance that the Wassenaar Agreement will become public after 2002. In April 2002 the Joint Committee, established through the Agreement, will hold her last session in Indonesia and will be dissolved on 31 May 2002, after 50 years of Moluccan
- sojourn in the Netherlands and 30 years of existence of the Joint Committee. In 2003 all the documents, regarding the Agreement and the Joint Committee, will be handed over to the Rijksarchief (Public Record Office).
- 15 Actually after the siege of the Indonesian Residence in 1970 a Joint Committee was formed, which negotiated the Wassenaar Agreement. The Wassenaar Agreement confirmed the need of a Joint Committee to conduct the implementation of the Agreement.
- 16 *Tweede Kamer der Staten-Generaal, Zitting 1974-1975, 13286, Beleid ten aanzien van in Nederland verblijvende Molukkers. Nr. 1. Verslag van een mondeling overleg. Vastgesteld 3 Februari 1975* (Second Chamber of the States General, Session 1974-1975, 13286, Policy toward the Moluccans staying in the Netherlands. Nr. 1. Report of an oral deliberation. Determined on 3 February 1975).
- 17 *Brief van de Vice-Minister-President (Hans Wiegel, R.A.) aan de Voorzitter van de Tweede Kamer der Staten-Generaal. 's-Gravenhage, 26 Januari 1978. Aanbieding Regeringsnota "De problematiek van de Molukse minderheid in Nederland." Hoofdstuk 6. De dialoog Molukkers-Indonesische samenleving.* (Letter of the Vice-Minister-President [Hans Wiegel, RA] to the Speaker of the Second Chamber of the Parliament. The Hague, 26 January 1978. Presentation of the Governmental Note "The problems of the Moluccan minority in the Netherlands." Chapter 6. The dialogue Moluccan-Indonesian society.)
- 18 Joop de Jong, "De Nederland-Indonesische relaties 1949-1999" (The Dutch-Indonesian Relations 1949-1999). In Martin Elands, ed., *Uit Indonesië. De erfenis van de soevereiniteitsoverdracht* (From Indonesia. The heritage of the transfer of sovereignty) (The Hague: SDU, 2000), 10-48.
- 19 Moluccans got the possibility to visit the Moluccas in groups (package tours) so that the Indonesian Authorities had the opportunity to exert control over the participants. One of the problems was the status of a number of Moluccan participants, who refused to accept the Dutch citizenship and, therefore, became stateless. But stateless Moluccans were synonym with the RMS. By handing over passports to those Moluccans the Indonesian Authorities lost their control over them. Al-

though this caused problematic discussions in the Joint Committee, the issue worked out of itself.

- 20 These myths were closely connected with 'a deterioration in the Dutch-Indonesian relations, in which anti-Dutch and nationalistic emotions on the side of Indonesia and an increasing rancour on the Dutch side were aggravated. (.....) A lot of the rancour of the Moluccan group, which in 1951 came to the Netherlands for a temporary stay, dates to this period.' See, Joop de Jong. 'Een inktzwarte bladzijde in de geschiedenis.' *Nederland en de Indonesische kwestie 1945-1950* ('A black page in history.' *The Netherlands and the Indonesian issue 1945-1950*). In: *Achtste jaarboek van het Rijksinstituut voor Oorlogsdocumentatie* (Eights Yearbook of the Governmental Institution for War Documentation) (1997), 76.
- 21 This research was in 1976/77 executed by De Muralt, but was not published. The results, however, were included in the appendices of the note of 26 January 1978 (see footnote 17).
- 22 The title of the Report was: 'De Ronde Tafel-conferentie, een overzicht van onderhandelingen met betrekking tot het zelfbeschikingsrecht der volkeren, het standpunt der Nederlandse regering en de reactie van de Tweede Kamer' (The Round Table Conference, an overview of the negotiations regarding the right of self-determination of peoples, the point of view of the Netherlands Government and the reply of the Second Chamber), popularly known as 'Dossier Ambon 1950.' See, E.I. van der Meulen. *Dossier Ambon 1950. De houding van Nederland ten opzichte van Ambon en de RMS* (Dossier Ambon 1950. The attitude of the Netherlands with respect to Ambon and the RMS). The Hague: Staatsuitgeverij, 1981.
- 23 Letter of Badan Persatuan (Rajat Maluku Selatan) of the Chairman S. Metiarj and the Secretary W. Munster, 23 February 1982, to the Netherlands Government, attention the Prime Minister.
- 24 See, Steijlen, F., *RMS: van ideaal tot symbool. Moluks nationalisme in Nederland 1951-1994* (From ideal to symbol. Moluccan nationalism in the Netherlands 1951-1994), Amsterdam: Het Spinhuis, 1996, 140-143.
- 25 Republik Maluku Selatan (22 November 1980). *Note of Protest to the CSCE in Madrid*. Marinho, 81, Nr. 1. In this Note of Protest the RMS indeed did not accuse the Netherlands of

violating Moluccan Human Rights as in a letter to the CSCE of the National Committee South Moluccan (*Landelijk Comité Zuid-Molukken*). Quote: 'But since the deportation of a part of the South Moluccan People to the Netherlands in 1951, the Dutch Governments have, in order to be able to withdraw from their obligation towards this people in a cunning way, pursued a policy aiming at genocide by:

- Demolishing and dismantling the Moluccan Advisory Council and other Moluccan (welfare) institutions;
- Scattering the people, which in fact threatens the existence and the further development of the culture and the identity of the South Moluccan community;
- Financing and promoting so-called "journeys of orientation" to the South Moluccas for various groups, obviously in the hope that this will eventually popularise repatriation;
- Playing a Nationality Law, which automatically incorporates the Moluccans who are born in the Netherlands into the Dutch nation;
- Using an official Governmental version of the South Moluccan history, which is completely based on the version of the Indonesian propaganda apparatus.

This policy of assimilation or repatriation, decentralisation and falsification of history is in violation of the Declaration Of Human Rights and the United Nations Charter!' (Capitals in the original document, R.A.)

- 26 An address to the Fourth Committee of the United Nations General Assembly by Dr. J. Alvarez Manusama, November 1982. To underline his suggestion of a revision of the decolonization of Indonesia Manusama referred, without mentioning the Moluccas in his address, to a letter of Husaini Hassan, chairman of the delegation of the Republic of Aceh, to the Special Committee on the Situation with regard to the Implementation of the Declaration of the Granting of Independence to Colonial Countries and Peoples.
- 27 Quote: 'Today Indonesia, Mr. President, Indonesia is behaving and conducting a policy as Adolf Hitler did about fifty years ago.'
- 28 *Nieuwsblad van het Noorden*, 15 March 1978: Member of Parliament van Leijenhorst after visit: 'RMS does not live on in the Moluccas.'

- 29 Commissie van Overleg Zuid-Molukkers Nederlanders (1978), *De Ronde-tafelconferentie. Een overzicht van de onderhandelingen met betrekking tot het zelfbeschikingsrecht der volkeren, het standpunt der Nederlandse regering en de reactie van de Tweede Kamer*, p. 3. (Commission of Consultation South-Moluccans-Dutchmen (1978), *The Round-table Conference*. An overview of the negotiations regarding the right on self-determination of peoples, the point of view of the Dutch Government and the reaction of the Second Chamber, p. 3.)
- 30 *De Limburger*, 10 April 1980: 'Van Agt avoids Ambon: South-Moluccans are angry.' For the Policy paper of the Government see note 16.
- 31 Also in the United States such voices could be heard: *Boston Mass Globe*, 30 Augustus 1980. Quote: 'In 1975 South Moluccans occupied the Indonesian consulate in Amsterdam. In 1977 they "hijacked" a school where they held more than 100 children hostage for days. Neither of these ploys gained anything. In fact, the only strategy that had any effect was the 1977 train hijack in which six South Moluccans died.'
- 32 *Algemeen Dagblad*, 19 April 1980: 'Unrest under Moluccans remains.' Quote: 'Yesterday night Manusama said that Van Agt "is grossly mistaken," if he thinks that the Moluccan issue will be solved through orientation visits. There were "orientation visits, excellent, but what is the result? That the visitors will give up their ideals of independence? On the contrary, mr Mantouw and Kukuwael, for example, don't think differently about independence. The unrest continues." Manusama stated. According to the Moluccan leader the Indonesian Government has serious problems in the Moluccas, as well as in New Guinea (Papua), Timor and Aceh.'
- 33 Actually for the Moluccas, the first major event came between February and April 1998, when the Moluccan Muslim leader in Jakarta, Deddy Hamdan, disappeared along with other pro-democracy activists. The elite force of the Indonesian army, Kopassus, was implicated in the kidnapping. Moreover, on 22 November 1998 violent clashes between Christian Moluccans and Muslims took place in Jakarta.
- 34 The social balance in the Moluccas was disturbed by the transmigration policy of the Soeharto regime. Transmigrants of other islands came to the Moluccas, many of them from Sulawesi. As a consequence the Christians Moluccans became a minority in that region. Moreover in the administration the better-educated Christian Moluccas, a heritage of Dutch colonialism, were replaced by Muslims. Although the Moluccans did not consider religion as a problem -the local adat system (Pela) included many Muslim and Christian relationships and co-operation- the disturbance of the social equilibrium the religious factor in the conflict grew.
- 35 On the one hand, the adversaries of the then president Abdurahman Wahid used the conflict to undermine his authority, on the other hand the policy of the president was muddled due to his inconsistent behaviour. Still the situation in the Moluccas is very tense and it presents the opportunity to weaken the position of president Megawati. See for an assessment of the Wahid Government *vis-à-vis* the Moluccas the report of the International Crisis Group (19 December 2000), *Indonesia: overcoming Murder and Chaos in Maluku*. ICG Asia Report No. 10. Jakarta/Brussels. Quotation: 'Meanwhile the weak elected government of President Abdurrahman Wahid remains incapable of asserting its authority in the Maluku region.' (p. 23)
- 36 Ministry of Foreign Affairs (November 2000), *Rapport EU-missie Molukken*, (Report of the EU-mission to the Moluccas). Message to the President of the Second Chamber.
- 37 *Bulletin EU* 10-2000 Common Foreign and Security Policy (17/26)
- 38 Ministry of Foreign Affairs (15 March 2001), *Verslag tweede missie naar de Molukken* (Report of the Second Mission to the Moluccas). Message to the President of the Second Chamber.
- 39 A mission to study the situation in conflict areas in Indonesia is organised in order to make an assessment of current and potential conflict situations, to review existing policies and measures to prevent conflicts, to propose medium-term objectives and to assess how these objectives might be integrated into the development priorities. Members of the mission will visit Indonesia in January and February 2002 under the responsibility

- of the European Commission. The mission will also visit the Moluccas as well as Aceh and Papua. The team of the mission shall also propose immediate short-term measures that can be supported under the European Community's Rapid Reaction Mechanism. See: Terms of reference for the deployment of a rapid assessment team in Indonesia, mimeograph.
- 40 Up to 28 June 2000 the Dutch emergency aid through several programs of various organizations has amounted to about 11 million Dutch guilders. In: Ministry of Foreign Affairs (28 June 2000), *Noodhulp Molukken* (Emergency Aid Moluccas). Message to the Speaker of the Second Chamber. Main argument for choosing the United Nations Organization UNDP was the role of co-ordinator of the UNDP in channelling aid by WFP, UNICEF, UNCHR, Action contre la Faim, Artsen zonder Grenzen België (Doctors Without Borders Belgium), and TIRUS, a platform of locally based NGO's. The Dutch Government considered the UNDP and other UN organizations and NGO's also important 'eyes' which could monitor the situation in the Moluccas, as long as international observers were not accepted by the Indonesian authorities. An overview of humanitarian aid to the Moluccas 1999 up to 2001 inclusive can be obtained from the Ministry of Foreign Affairs, *Geografisch overzicht Humanitaire Hulp op de Molukken* (Geographical overview Humanitarian Aid in the Moluccas), mimeograph.
 - 41 The inactivity of the Dutch chairmanship of the Security Council with respect to the Moluccan issue was mainly caused by the general Dutch attitude, seconded by the members of the Council, that the conflict was an internal Indonesian matter. Although the Second Chamber also urged the Minister of Foreign Affairs to put the Moluccan issue on the agenda of the Security Council, he refused to do so, because this would harm the fragile position of the Indonesian Government due to a lack of confidence in President Wahid. See: *NRC Handelsblad*, 29 June 2000.
 - 42 Ministry of Foreign Affairs (24 August 2000), *Werkzaamheden Veiligheidsraad/Juli 2000* (Activities of the Security Council/July 2000). Message to the Speaker of the Second Chamber.
 - 43 As was the case with the conflict in the Seventies the Timor issue was again high on the agenda, due to the Indonesian actions in East-Timor and the referendum about the independence.
 - 44 Ministry of Foreign Affairs (27 June 2000), *Situatie op de Molukken* (Situation in the Moluccas). Message to the President of the Second Chamber. Answer of the Minister of Foreign Affairs with reference to a letter of the Speaker of the Second Chamber, 20 June 2000, Nr. 200044, together with a request of the MP Koenders (Labour Party) about the situation in the Moluccas. See also, Ministry of Foreign Affairs (December 2000), *Uw verzoek BUZA 2001/99 m.b.t. recente ontwikkelingen in Indonesie* (Your request BUZA 2001/99 regarding recent developments in Indonesia). Message to the Chairman of the Permanent Commission for Foreign Affairs of the Second Chamber. Nr. DAO-1193-01.
 - 45 The Minister of Foreign Affairs also received regularly questions of members of the Second Chamber of the House of Parliament about the situation in the Moluccas and the contacts with the Indonesian Authorities. In particular the MPs Bert Koenders and Usman Santi, both of the Labour Party (the biggest governmental party), the latter also member of the Moluccan Community, were very active in asking questions of the minister. See among others: *Written Questions* regarding the Moluccas of the Members Koenders and Santi, submitted the 17th of December 2001,, Nr. 2010203660.
 - 46 The letter of the Minister of Foreign Affairs Jozias van Aartsen to his Indonesian colleague Alwi Shihab was dated 30 December 1999.
 - 47 Such intervention was perceived as an undermining of the authority of President Wahid, which was not in the interest of Indonesia and the International Community. Intervention by member states of ASEAN also encountered rejection among the ASEAN countries, of some of which are dealing with comparable problems.
 - 48 This workshop was the start of a series of workshops followed by a special course for military people in the Hague at the Clingendael Institute, February 2002.
 - 49 From 21-22 February 2001 Christian and Muslim representatives from the Moluccas

- met with Christian and Muslim representatives of the Moluccan Community in the Netherlands at the Clingendael Institute in the Hague in co-operation with the Management Team Dialogue of the Moluccan Churches: Seminar: *De Molukken. Hoe kunnen vrede en samenwerking bereikt worden?*/Seminar: *Maluku. Bagaimana mewujudkan damai dan kerja sama?* (Seminar: the Moluccas. How to achieve Peace and Co-operation?)
- 50 A good and comprehensive overview of the interactions between the acts of violence in the Moluccas and the acts of the Dutch Government can be found in: Bosch, Tanja van den, *Ikut Campur. Een onderzoek naar de mate van beïnvloeding door de Molukse gemeenschap in Nederland op het beleid van de Nederlandse overheid, de EU en de VN ten aanzien van de oorlog op de Molukken*. MA Thesis, University of Twente, 2001 (*Ikut Campur. A study into the amount of influence by the Moluccan Community on the policy of the Dutch Government, the EU and UN with respect to the war in the Moluccas*.) A second informative MA Thesis dealing with the issue, in particular with respect to the influence of the media is: Chiu, W.J. (2000), '*De Pen, het Publiek, en de Politiek.*' een onderzoek naar de relatie tussen de berichtgeving in de media, de publieke opinie en de Nederlandse interventiepolitiek inzake het geweld in de Molukken in 1999. University of Twente. ('The Pen, the Audience, and the Politics,' a survey of the relationship between reporting news by the media, public opinion and Dutch intervention policy on the subject of the violence in the Moluccas in 1999.) See also: Fridus Steijlen, 'Politieke invloed en Molukse netwerken' (Political influence and Moluccan networks). In, Thijl Sunier, et al., eds., *Emancipatie en subcultuur. Sociale bewegingen in België en Nederland* (Emancipation and subculture. Social movements in Belgium and the Netherlands). (Amsterdam: Instituut voor Publieke en Politiek, 2000), 122-137.
 - 51 For an extensive list of activities regarding the Moluccan Community in light of the conflict in the Moluccas of both ministries from December 1998 through June 2001 see: www.ministervanboxtel.nl/sites/ministervanboxtel/contents/i000409/overzicht_activ_molukken_10-00.pdf and Ikut Campur, opus cit.
 - 52 Ministry of Foreign Affairs (June 2000), "Indonesië Notitie" (Indonesian Paper). In: Ministry of Foreign Affairs (28 June 2000), *Noodhulp Molukken* (Emergency Aid Moluccas). Message to the President of the Second Chamber.
 - 53 Ibid.
 - 54 The Dutch fear of transfer of the Moluccan conflict to the Moluccan Community in the Netherlands was understandable, although the situation in the Moluccas had changed dramatically under Indonesian rule as well as in the Netherlands. However, in the Netherlands, too, the Moluccans were rather heterogeneous and an internally divided community. The members of the Moluccan Community come from different parts of the Moluccas; they have different religious backgrounds and their culture can be characterised by a strong particularism, in addition to the various relationships between relatives, families and kinship, the village and the island, as well as the so-called 'Pela-relationships'. See among others: J.E. Ellemers, 1978, *Minderheden en beleid in Nederland: Molukkers en enkele andere categorieën allochtonen in vergelijkend perspectief* (Minorities and policy in the Netherlands: Moluccans and some other categories of migrant groups in a comparative perspective). In *Transaktie 7*, no. 1: 20-40.
 - 55 i.e. Repatriation of first generation Moluccans, financing small utility projects in the villages of the repatriates and facilitating exchange between the Moluccan communities.
 - 56 *NRC Handelsblad*, Kok achter Molukkers (Kok backing the Moluccans), 10 June 2000.
 - 57 Paul Patty, the spokesman of the Free Moluccan Youth, made these statements. See: *NRC Handelsblad*, 8 September 2000. The affair blew over with a conviction of 80 hours work penalty. See: *ANP*, 5 May 2001.
 - 58 The spokesman for both organizations was the Moluccan Leo Reawaruw. The Home Security Police (BVD) wrote in its Annual Report 2000 (page 27): 'Mid-September he called into existence the action group People Against Genocide (PAG), of which he acted as spokesman, but in fact he was the only member. (...) At the beginning of December this Moluccan told reporters that a new radical splinter group, called Maluku Warchild, had separated itself from PAG.' The publicity around Maluku Warchild, however, caused societal and political commotion. Ironically the Dutch Telecom (KPN) launched

a campaign 'KPN Telecom. Supporter of all soccer players' with a group portrait of amateur soccer players. One of them in the picture was Reawaruw, who played with the veterans of an amateur soccer club. The KPN removed all the posters after the name of Reawaruw was revealed as a political activist.

59 *De Volkskrant*, 2 August 2001.

60 *Het Parool*, 18 September 2000.

61 Present were the Prime Minister, the Minister of Foreign Affairs and the Minister for Big Cities and Integration Policy. This talk with Moluccan organizations was the second one. The first talk took place in September 1999.

62 *NRC Handelsblad*, 17 October 2000.

63 *Trouw*, 2 February 2001.

64 The program is still under construction with the assistance of the Moluccan Historical Museum and the Clingendael Institute.

65 It can be ascertained that 'the better immigrant organizations are officially recognised and addressed upon their bridge-function, the more is the chance that they will function as binding agents in the integration process.' In: Rinus Pennix and Marlou Schrover, *Bastion of bindmiddel? Organisaties van immigranten in historisch perspectief* (Bastion or binding agent? Organizations of immigrants in a historical perspective). (Amsterdam: Institute for Migrant and Ethnic Studies (IMES), 2001), 57. The Dutch Government established among others in 1976 the *Inspraakorgaan Welzijn Molukkers* (Participation Organ Welfare Moluccans) succeeded by the *Landelijk Overlegorgaan Welzijn Molukkers* (National Organ Welfare Moluccans; LOWM). In 1986 when the *Badan Persatuan* concluded a *Gezamenlijke Verklaring* (Joint Declaration) with the Dutch Government which included the establishment of the Moluccan Historical Museum and the National Support-

center for Moluccan Education (LSEM). The Government also endowed the Moluccan Churches, so they could build a Moluccan Church Center in Houten near the city of Utrecht.

66 See for more general remarks about institutions in highly developed countries: Easterly, William (2001), *Can Institutions Resolve Ethnic Conflict?* New York, Mimeo, World Bank, p. 12.

67 The valuation of the influence of the RMS on the Moluccan Community and on the civil war in the Moluccas is rather sceptical. The visit of the Moluccan delegation to the then president Wahid, which also included the participation of the RMS, did not have a demonstrable effect. Also the re-declaration of the RMS in the Moluccas by the Front Kedaualatan Maluku (a Dutch-Moluccan co-operation) did not gain much sympathy both in the Netherlands and in the Moluccas. See, for example, Fridus Steijlen, *Kerusuhan. Het misverstand over de Molukse onrust* (Kerusuhan. The misunderstanding of the Moluccan unrest). (Utrecht: Forum, 2001), 31-34. Steijlen is of the opinion that the FMK-meetings could become 'a potential catalyst for political action, because the organization uses an ideological rhetoric that many will recognize.' However, after a brief uproar the whole action turned out to be in vein.

68 Tanja van den Bosch, *Ikut Campur. Een onderzoek naar de mate van beïnvloeding door de Molukse gemeenschap in Nederland op het beleid van de Nederlandse overheid, de EU en de VN ten aanzien van de oorlog op de Molukken*. MA Thesis, University of Twente, 2001 (Ikut Campur. A study into the amount of influence by the Moluccan Community in the policy of the Dutch Government, the EU and UN with respect to the war in the Moluccas.), p. 93.

69 *Kompas*, 13 February 2002.

The Indonesian Crisis from '*Krismon*' to '*Kristal*'

Perceptions of Social and Cultural Impact in Jakarta and Semarang

Yasmin Sungkar

BACKGROUND

THROUGHOUT the 1980s and much of the 1990s, Indonesia enjoyed high rates of economic growth, a reduction in poverty and improvements in the health and education of the population. Expectations that this rapid growth would continue vanished in mid-1997 when the currency crisis began to sweep Southeast Asia. The immensity and unanticipated nature of the crisis are particularly remarkable when contrasted with the country's recent economic success. In July 1997, following the decline of Thai Baht, the Indonesian Rupiah fell dramatically. As the rupiah slid, enormous private sector debts emerged and the banking sector was paralyzed by a high level of bad debt. Because Indonesian companies had borrowed heavily in dollars to benefit from lower interest rates,¹ the rupiah's

dramatic drop steeply increased the cost of repaying Indonesia's huge commercial and government debts. The rupiah has been subject to large swings, prices of some goods have risen extensively, and billions of dollars have been loaned by international lending organizations. The Indonesian economy has undergone tremendous change since then.

The crisis also sharply increased the prices of imported raw materials and basic foods. The ability of many exporters to borrow US dollars, which they needed to pay for imported raw materials, shrunk along with the value of the rupiah. Local banks became reluctant to lend because they did not want to risk another currency plunge or a borrower going bankrupt between the time an exporter bought raw materials and got paid for finished goods. Domestic banks were in any case weighed down by burden of bad loans. Not surprisingly, numerous banks were seriously undercapitalized, and some even insolvent. In early November 1997, the central bank closed 16 banks that were completely insolvent or in

¹Indonesian businesses have long complained that domestic interest rates are the highest in ASEAN, leading corporate borrowers to the international markets.

particularly serious jeopardy.² The rationale was to demonstrate the government's determination to deal decisively with financially troubled banks. Instead, the action led to a loss of confidence in the rest of the banking system. With each plunge of the rupiah, the price of chicken rose due to the higher cost of imported feed. Noodles made with imported flour cost more.³ Public insecurities mounted, sparking the political fires later to engulf Soeharto.

The Indonesian monetary crisis or '*krismon*' (*krisis moneter*), which later became a political and social crisis or '*kristal*' (*Krisis politik dan sosial*) as well, had seen the growth rate drop from 8% —the average annual growth rate from 1970 to 1996— into -(minus)14% in 1998. The government's fiscal position deteriorated as well. By mid-1998 Jakarta was running a budget deficit of 8.5%, largely to fund social sector safety nets in the form of subsidies. The budget's priorities made clear that the government's concern for ensuring social stability often overrode desires to conform to an IMF blueprint. In addition to the currency crisis, the nation experienced its worst drought in 50 years, causing famine. To restrain potential social unrest, the nation's petroleum subsidy was increased. Total subsidies to Indonesia's regions increased by 7% to Rp 12 trillion, while total development expenditures increased by 6% to Rp 41 trillion.⁴

The debate over the crisis centered on the link between currency depreciation and economic fundamentals. One view suggested that Indonesia's economic fundamentals were as sound as they had ever been, and were more sound than those in Thailand. Thus the large depreciation must have been caused by other factors, such as hedge funds.⁵ Clearly, dynamics in global capital markets had precipitated the crisis but why was the impact on Indonesia so devastating? Others argued that the large depreciation was evidence that Indonesia's economic fundamentals were much less sound than was generally believed, and that the public had not been sufficiently informed of the real state of the economy. In January 1998, the Indonesian rupiah dropped more than 70% against the US dollar. Set against the widely acknowledged strength of the nation's economy, such disparity intuitively signaled a monetary problem.⁶

In his State Address delivered to the Parliament on 16 August 1997, President Soeharto said, "We live in a world that is changing fast, a world that seems to be moving toward a great economic union. Very often events in one country or region immediately influence other countries or regions. The World Community is entering a new era, an era characterized by an open world economy and trade".⁷ Many in Indonesia's crisis-management

²The Jakarta Post, 2 November 1997.

³The New York Times, 9 January 1998.

⁴The Wall Street Journal, 8 January 1998.

⁵Hadi Soesastro and M.C. Basri, 'Survey of Recent Development,' *Bulletin of Indonesian Economic Studies* 34, no. 1 (1998): 5.

⁶The Wall Street Journal, 9 January 1998.

⁷The Jakarta Post, 4 November 1997.

team formed in August 1998 believed that the smooth operation of the Indonesian economy previous to the current crisis had allowed Soeharto to put off dismantling monopolies as well as carrying out other reforms that were essential to restoring confidence.⁸ They saw domestic causes for Indonesia's crisis rather than just a macroeconomic contagion brought on by regional events.⁹ The fact that the currency crisis in Indonesia began in the wake of problems affecting other countries in the region should not in their view be an excuse. Its origins are both domestic and external. On the one hand, orthodox economists saw domestic origins lying in policy mistakes. Soesastro and Basri pointed out three domestic factors that contributed to the current crisis. *First*, government failure to dampen overheating pressures. *Second*, maintenance of pegged exchange rates or predictable rates of depreciation (as in the case of Indonesia), which encouraged inadequately hedged external borrowing by both the financial and the corporate sectors. And *third*, weak prudential regulations and financial oversight that led to a sharp deterioration in the quality of bank loan portfolios.¹⁰ On the other hand, Robison and

Rosser argue that the origin of the crisis was related to important shifts in political and social power during the 1980s, realignments that involved the emergence of powerful coalitions of private business interests, bureaucrats and politicians.¹¹ The crisis therefore shattered the political and economic relationships that had cemented Indonesia's economic regimes, opening the way for reform.

In addition, political uncertainties, lack of transparency, and loss of confidence in successive governments have all heightened the crisis. Paul Krugman argues that the currency crisis is a symptom rather than the cause of a wider financial crisis, caused by excesses in financial intermediation and the associated 'moral hazard' of a poorly regulated financial system. The problem is off the government's balance sheet and is mainly in the private sector. Jeffrey Sachs has made the same point. Weak prudential regulations and government interventions in the allocation of bank credits, through government guarantees or other means, have helped establish widespread bad banking practices.¹²

Given the extent of the decline in real GDP in 1998, the debate about the impact of the country's crisis was, and continues to be, very intense in Indonesia. The government was under immense pressure to

⁸The team is an impressive line-up of old policy-makers with a distinctly reformist economic bent: Finance Minister Mar'ie Muhammad, Bank Indonesia Governor Sudradjad Djiwandono, State Secretary Moerdiono, presidential advisers Widdiodjo Nitisastro, Ali Wardhana, and Saleh Afiff.

⁹*Far Eastern Economic Review*, 4 September 1997, 62.

¹⁰Hadi Soesastro and M.C. Basri, 'Survey of Recent Development,' *Bulletin of Indonesian Economic Studies* 34, no. 1 (1998): 6.

¹¹Richard Robison and Andrew Rosser, 'Contesting Reform: Indonesia's New Order and the IMF,' *World Development* 26, no. 8 (1998): 1595.

¹²*The International Herald Tribune*, 6 November 1997.

take action to alleviate various emerging problems when the effects of both the financial crisis and the severe drought were becoming apparent. Action was necessary even if there was no imposing evidence that the target beneficiaries were those most severely affected by the crisis. With the assistance of the World Bank and AusAID, a Social Monitoring and Early Response Unit (SMERU) was established in late 1998 to coordinate work on the effects of the crisis and to examine the effectiveness of government intervention programs.

Several studies have examined the social impact of the crisis. World Bank officials were quoted as stating that the middle classes in urban areas had taken the most severe blow of the crisis, and that young, relatively well-educated workers had suffered far greater income declines than the least educated and poorest workers in rural areas. The report acknowledged that many people who had lost relatively well-paid jobs in the formal sector had been pushed into less stable and less profitable work in the informal sector. The Rand study found that the percentage of people in poverty had risen from around 11% in 1997 to between 14% and 20% in 1998.¹³ The Nationwide Kecamatan Survey—the most comprehensive survey in terms of geo-

graphy— contributed three main findings. *First*, urban areas have been harder hit by the crisis than rural areas. *Second*, the impact of the crisis is heterogeneous, with some regions experiencing great difficulties and others doing relatively well. *Third*, there is little connection between initial poverty levels and the extent to which an area has been hit by the crisis, with some relatively poor areas have not been hard hit while some relatively well off areas have been quite hard hit.¹⁴

The study examined the immediate effects of the Indonesian crisis on labor market outcomes using two rounds of Indonesia Family Life Survey (IFLS)—a longitudinal survey collected in 1997 and 1998— rejected the prediction that the Indonesian crisis would be accompanied by massive unemployment. It concluded that the drama of the crisis is not reflected in unemployment but rather in the devastation it has had on earnings. On average, real hourly earnings declined by over 40% between 1997 and 1998.¹⁵ The study analyzed price changes and the poor found that prices varied substantially across the disparate regions of Indonesia. Prices also varied across the type of goods considered. On top of this variation, con-

¹³ Anne Booth, 'The Impact of the Indonesian Crisis on Welfare: What Do We Know Two Years On?', in *Indonesia in Transition: Social Aspects of Reformasi and Crisis*, edited by Chris Manning and Peter van Diermen (Singapore: ISEAS, 2000).

¹⁴ Sudarno Sumarto, Anna Wetterberg, and Lant Pritchett, *The Social Impact of the Crisis in Indonesia: Results from a Nationwide Kecamatan Survey*.

¹⁵ Thomas Duncan, Kathleen Beegle, and Elizabeth Frankenberg, *Labor Market Transition of Men and Women During an Economic Crisis: Evidence from Indonesia*, August 2000.

sumption patterns varied both regionally as well as by income class. Of all households, the urban poor appeared the most adversely impacted by the crisis. Their cost-of-living tended to rise the most and, being poor, these households are presumably among the least able to absorb these increases.¹⁶

This paper presents part of survey results investigating the impact of the economic and financial crisis on the society and cultures in Southeast Asia. The survey is sponsored by the Korean National Commission for UNESCO and The Korea Research Foundation and organized by the Korean Association of Southeast Asian Studies and the Institute for East Asian Studies, Sogang University. The purpose of this survey is to understand how and to what extent people are affected by economic problems. The survey was designed to capture a detailed picture of people's perceptions of various issues, including: the economic condition of their personal life and their nation in general; their government's policy in handling the economic crisis; the recovery process; and the effect of the crisis on their own employment, households, education and relationships among family, friends, and neighbors. In addition, the survey also tried to capture the social and cultural attitudes and to measure confidence levels in various institutions.

SURVEY METHODOLOGY

The Indonesian survey was not designed to be nationally representative. Rather, it was focused disproportionately on two cities — Jakarta and Semarang. Hence, it is not appropriate to generalize the specific results generated here to the country at large without qualification. Nonetheless, recognizing this limitation, there is no immediate evidence to suggest that these results are anomalous, or that results would radically differ in other regions of Indonesia.

The survey comprised purposive samples from both cities. Five areas in Jakarta were selected and 50 respondents were randomly chosen in each area. These are: two middle class areas (Tebet in South Jakarta and Palmerah in West Jakarta); two working class areas (Koja in North Jakarta and Cakung in East Jakarta); and one poor district (Kampung Melayu/Bukit Duri on the border of Central and East Jakarta). While the survey conducted in Semarang does not exactly mirror the Jakarta pattern, it contains the same number of respondents. Some other respondents were also randomly chosen. Those were: 50 middle class respondents (in Gajah Mungkur and Wonotingal); 50 working class respondents (in Mangunharjo and Tinjomoyo); 50 respondents in poor areas (Bandarharjo and Sadeng); and 100 respondents from two rural areas (Mranggen and Pringapus). In total, the survey covered 13 locations (five locations in Jakarta and eight locations in Semarang) involving 150 middle class respondents, 150 working class respondents,

¹⁶James Levinsohn, Steven Berry, and Jed Friedman, *Impacts of the Indonesian Economic Crisis: Price Changes and the Poor*, 1999.

100 poor class respondents, and 100 rural area respondents.

Those respondents—who were respectively the head of household—were asked a standard set of questions about the social and cultural impacts of the economic crisis. The questions were divided into five groups: (1) General Conditions, which consist of both personal life and the country as a whole; (2) Economic Crisis and Government Policy; (3) Impacts of the Economic Crisis on Personal Life; (4) Ideologies and Values; and, (5) Institutional Confidence.

The *first* group of questions, i.e., General Conditions, is aimed at getting the respondent's perceptions of general conditions at present and those likely to occur in the next two years, as well as important concerns he may have.¹⁷ The same questions apply to both personal life and the whole country. The *second* group of questions, i.e., Economic Crisis and Government Policy, is intended to get the respondent's perceptions of the sources of the crisis and the economic recovery process. The *third* group of questions, i.e., Impacts of Economic Crisis on Personal Life, covers significantly broader issues designed to measure the degree of change in income, expense, job, education, food consumption, as well as relationships among family members, neighbors and friends. The *fourth* group of questions, i.e., Ideologies and Values, consists of a series of hypothetical questions in-

tended to measure the respondent's agreement with various social and cultural attitudes. The *fifth* group of questions, i.e., Institutional Confidence, is aimed at measuring the respondent's confidence level in different institutions.

There are limitations to every approach; and the use of subjective qualitative questions is no exception. With the decision to use this type of instrument, the loss of quantitative precision and the reliance on a small number of respondents in each location were the price paid for a rapid survey. A qualitative survey using a purposive sampling approach was chosen since a quantitative survey demands region sample sizes that are simply too large. By asking for qualitative assessments we hoped to get regional coverage with complete responses of people's perceptions of the impacts of the crisis. It was also necessary to limit the number of respondents in each area to minimize the time discrepancy between survey period and data presentation given the rapid and unpredictable rate of change presently seen in Indonesia.

SURVEY RESULTS

Personal Life and General Conditions of the Country

From 500 respondents: 47.6% of them are satisfied with the way things are going now in their personal lives, while those dissatisfied number 44.4%. Considering the serious impact of a crisis now in its fourth year, these results seem mystifying. The key to the paradox may be the culture

¹⁷The use of the masculine pronoun in this paper refers to both genders; 71.1% of survey respondents were male and 28.5% were female.

of being '*nrimo*', Javanese acquiescence to fate. And in this result we found what may be the most significant variation from the likely results of a broader national survey beyond the island of Java.

Moreover, Amsterdam University sociologist Jan Breman, suggests that the impact of the crisis in rural areas is greater than in cities.¹⁸ This finding would support our survey results since only 20% of our respondents live in rural areas, thus their more negative perceptions would be weighted correspondingly lower than the 80% of non-rural respondents holding more positive views. Differing from Breman, Selo Soemardjan, a University of Indonesia sociologist, argues that the urban lower and poor classes were the first victims of the monetary crisis because these groups do not have the savings to support their lives while their expenses keep rising. He also concludes that the impact of the monetary crisis is generally more severe in large cities than in small cities or villages. This is because urban populations have a relatively high dependence on the US dollar and imported goods while the crises in agrarian areas were mainly caused by a long drought.¹⁹

¹⁸Prof. Dr Jan C Breman conducted research in several rural areas in West and Central Java eight years ago. His 1998 visit to the same locations found much greater levels of poverty, due principally to large scale layoffs in various formal sectors which caused unemployment flow to the villages. Together with rising prices of staples, the unemployed added to a social and economic burden in rural areas. *Kompas*, 17 April 1998.

¹⁹*Kompas*, 20 March 1998.

In contrast, 72.6% of respondents are dissatisfied with the way things are going now in the country. Given that the currency crisis has undermined the foundations of the financial and banking systems, caused a rapid rate of inflation, weakened purchasing power, caused mass layoffs, and evolved from a monetary crisis into a social, economic and political crisis, this result is not unexpected.

On the question of the most important concern about personal life, the answer is inflation (35.2%) followed by job security (15.4%) and income (12.2%). Inflation is the first thing that people worry about because the rupiah's dramatic drop immediately caused a substantial increase in the consumer price index, especially food.²⁰ At first glance, it may seem surprising that domestic food products are affected by exchange rates. The influences are indirect. For instance, chicken is not an imported good—not directly related to the free fall of exchange rate in rupiah—but chicken feed is an imported good, and rises in feed prices led to rises in poultry prices. The same principle applied to instant noodles and tempefavourite foods among the majority of Indonesians, hence the conclusion by Levinshon et.al., that price increases have impacted the cost-of-living of poor households disproportionately hard.

²⁰Given the great amount of devaluation during 1998, the price of traded goods, especially food, had risen more rapidly than the price of non-traded goods such as housing. The composite 44-city consumer price index showed that by January 1999, food prices had risen 133% compared with December 1997, whereas housing prices had risen by 49%. BPS, 1999.

It is interesting to note the difference in response when people were asked about their most important concern for the country. First was crime (16.6%) followed by political leadership (12.6%), and religion and morality (11.2%). These concerns again mirror the reality of Indonesian daily life for the last three years. With many of the poorest in society seeing no way to survive but through petty crime (and worse), and the breakdown of judicial processes that resulted in increasing instances of mob justice, the rule of law is now absent in many areas. After the fall of Soeharto, neither the Habibie administration nor Wahid's government were able to lead the country out of the crisis. These consecutive governments were likewise unable to solve religious and ethnic clashes in Maluku, Kalimantan, and Sulawesi. To the public eye, the most visible activity undertaken by these governments and various political figures has been merely an increasing grappling for personal advantage and political power.

Despite these social, economic, and political problems, 39.8% of respondents believe that their personal economic situation will improve in the next two years, and while 57% of respondents believe that the country's present economic condition is bad, it is interesting to find that 30.8% of them believe that the country's economic situation in the next two years will improve. It is reasonable to suspect that this optimism is primarily based on wishful thinking. In fact, the recovery process in Indonesia moves much slower than in Thailand and South Korea. It is too easy to forget that Indonesia faces a list of troubles beyond its economy —

chiefly environmental (forest fires, deforestation, rampant pollution), climatic (severe drought), and civil-political (separatist movements, sectarian violence), each becoming more problematic as the months pass.

Economic Crisis and the Government Policy

The set of questions in this section is mainly aimed at finding people's opinion on the issues of the source of the crisis, the government policy to overcome the crisis, and the recovery process. From 500 respondents, 42.8% deem the government as the most responsible for the crisis. Corruption is next — 34.2 %. Analytical debate over the source of the crisis has encompassed the issue of governance, with some analysts arguing that corruption and nepotism were responsible for the collapse in Indonesia. Many of the comments on the East Asian crisis of 1997-1998 were characterized by emphasis on the alleged wrongdoing of Asian governments. In particular, these critics have blamed governmental corruption for some of the unwise and inappropriate investment decisions of the 1990s. Undeniably there has been corruption in many Asian countries and in some, especially Indonesia, on a very large scale.

Despite the fact that government made an effort to ease the economic crisis through the social safety net,²¹ which includes

²¹Total budget allocated for social safety net program in 1998 is Rp17.5 billion. This program was funded by Asia Development Bank, World

food, employment, education, health and small business programs, the majority of respondents (68.6%) perceive that the country is not recovering from the economic crisis. Parallel to this opinion, 62.6% of respondents say that government policy in handling the economic crisis is inappropriate. Press reports in November 1998 asserted that only 30% of the total social safety net budget allocated for 1998 had been spent. According to Mubyarto—a proponent of a populist strain of economics currently working for the National Planning Agency—the social safety net program was attempted in a rush, without adequate planning or supervision. He further said that it was not appropriate to apply the same program across the country, ignoring the differing problems among regions.²²

Ultimately, however, the failure of the social safety net program surely occurred not only through bad planning, but also by having been turned into a “project”, a culturally understood reference (incorporating the ironic quotation marks when reported by the press) to describe something—especially a government program—from which one may gain personal benefit through corruption or collusion.

It comes as little surprise, then, that 80.6% of respondents assert that they did not receive any economic help from others since the economic crisis began in

1997. For those who received economic help, nearly half say they got help from relatives or friends—not from the government. This suggests that the historic ‘*gotong royong*’ principle—mutual help among extended families and communities—still applies in Indonesia. One wonders, of course, how much longer the poor can underwrite the poorer.

However, in a time of increasing nationalist sentiment, it is surprising to find that 45% of respondents say that international financial organizations, such as the International Monetary Fund (IMF) and the World Bank have been helpful to Indonesia. In its attempt to overcome the crisis, the Indonesian government was forced to seek the assistance of the IMF. However, the IMF’s macroeconomic prescription for Asia—higher interest rates, less government spending, higher taxes—was under attack. Joseph Stiglitz, chief economist at the World Bank, sees the Asia crisis as a crisis in confidence. He suggests that the IMF focus on “root causes” of the crisis, not on consequences that make it difficult to deal with.²³ A similar view is held by Ross McLeod, an Australian academic, who argues that the IMF has mishandled the Indonesian situation and taken the country from a bad economic crisis to a worse political crisis.²⁴ Controversy arose in 1998 over the use of IMF-organized loans. Kadin, the Indonesian Chamber of Commerce and Industry,

Bank, Unicef, and Indonesian state budget. *Kompas*, 24 February 1999.

²²*Kompas*, 29 November 1998, 12 February 1999.

²³*The Wall Street Journal*, 8 January 1998.

²⁴*The Jakarta Post*, 20 March 1998.

proposed that the disbursed funds be used to increase liquidity in the economy and to help smaller banks faced with liquidity problems.²⁵ Economist Rizal Ramli argued that the IMF loans not be used this way, as this would only increase the country's external debt burden. Instead he proposed that the government should declare a debt moratorium. A 'negotiating team' headed by former senior minister Radius Prawiro, was formed to consult and negotiate with the creditors. Prawiro's first statement was to reject the option of a debt moratorium.²⁶

Impacts of Economic Crisis on Personal Life

Concerning the severe impacts of the economic crisis, it is surprising to find that only 12.4% of respondents feel that their life has changed substantially whereas 37% say their life has not changed. The rest, 50% of respondents, answer that their life has changed slightly. These results suggest that the severity of the impact of the economic crisis was not uniform across different groups within cities and likely vary even more across the country. It is also possible that news media reports on the impact of the crisis were occasionally exaggerated. However, there is no doubt that the economic crisis increased the number of unemployed in Indonesia.

The highest rates of layoffs occurred as hyper depreciation of the rupiah against the US dollar led to the collapse of many industries, especially in the construction sector, banking and other formal sectors. In addition, dramatically higher interest rates contributed to the increase of unemployment as many industries could not afford the loans necessary to sustain production.²⁷

It can be concluded that only a small percentage of respondents in Jakarta and Semarang lost their jobs as a result of the crisis. The following findings support this conclusion. A big percentage, 71.8%, of respondents say that neither they nor anyone in their households lost a job since the economic crisis began in 1997. Furthermore, 92.8% of respondents answer that neither they nor their family have moved to another village or town because of financial difficulty. What has changed is income and purchasing power. While total household income stayed the same for 40.4% of respondents, it decreased for 38% of respondents. In contrast, 80.4% of respondents say that total household spending increased, a result of increased prices in basic foodstuffs. Despite the sharp increase in food prices, it is surprising

²⁵ *Bisnis Indonesia*, 22 November 1997.

²⁶ *The Wall Street Journal*, 9 January 1998.

²⁷ It was estimated that about 36,000 employees or 60% of total employees of the automotive industry were temporarily layoff. This is due to the high import component, almost 90%, in this industry which further forced a stop to production. PT Astra International, the biggest automotive company in Indonesia, stopped production for some time and did not renew the contracts of 4,000 contract worker. The company sustained huge losses — Rp 2792 billion in 1997 and Rp 2.26 trillion in the first three months of 1998. *Kompas*, 5 January 1998, 11 June 1998.

that 85% of respondents did not reduce the number of meals or cook fewer dishes. It is probable that many households substituted less expensive food items for more expensive ones. They are also likely to have cut back on non-food expenditures in order to maintain essential food purchases.

A certain degree of emotional sustenance is also required to cope with crisis. About 75% of respondents feel that their relationships among family, friends and neighbors stayed the same. About 22% of respondents say that their relationships have improved. Paradoxically, the widespread difficulties brought on by the economic crisis did not damage society in terms of social relationships but rather brought people into closer relationships. People believe that they share the same feelings about the crisis and encounter the same difficulties. This survey also finds that their participation in social gatherings and cultural ceremonies occurs about as often as before.

Ideologies and Values

In this category, respondents were asked to answer questions about social and cultural attitudes. Most respondents disagree with the following statements: (1) happiness in life is usually outside one's control; (2) religion divides people in Indonesia; (3) race and ethnicity divide people in Indonesia; (4) the main reason for poverty is laziness; and, (5) a man's ability differs according to race and ethnicity.

In other words, they believe that different religions, races and ethnicity within the country will not disunite people in Indonesia. It is also interesting to find that 58.4% of all respondents disagree with remark that Western developed countries in general are not helpful to developing countries, such as Indonesia. Thus, the emergence of nationalist sentiment may not widely reflect the views of a majority of Indonesians but rather reflect political positions promoted by certain groups exercising the major share of authority within the central government.

Conversely, most respondents agree with the following statements: (1) religion is the most important thing in life; (2) people should be free to choose his or her religion; (3) business is basically run for profit; (4) people in general are trustworthy; (5) education is the most important means for a country to develop economically; and, (6) politicians in general do not care about ordinary people. It is not difficult to understand why there is little faith in politicians. The hope shared by a majority of people that the fall of the New Order government would change the political climate in Indonesia has faded in the face of the protracted fight among the political elite to preserve their own interests — ignoring the huge problems affecting the ordinary citizens.

Institutional Confidence

The last category is a series of questions about how much trust or confidence —very

high, high, low, or very low— that people have in various institutions. Most respondents, between 42% and 59% of total respondents, have high trust or confidence in the following institutions: schools, hospitals, religious organizations, banks, labor unions, the civil service, and the military. After attributing much of the blame for the crisis to the government, it is surprising to discover that respondents in Jakarta and Semarang have high trust in banks, the civil service and the military. Despite the collapse of the banking system, inefficient as well as corrupt bureaucracies, and a military whose tendency to tread on civil liberties is notorious, people still have hope for these institutions. However, particularly regarding the military, this may reflect a tendency to seek tranquility in turbulent times, to remember only the relative stability and prosperity of the New Order era, not its less pleasant attributes.

In contrast, most people —between 40% and 51% of total respondents— have low trust or confidence in the following institutions: mass media, big companies, political parties, the judiciary, and political leaders. This can be understood since many big conglomerates —most of them associated with the Soeharto family— collapsed soon after the crisis hit, causing huge unemployment.²⁸ Their debts have also contributed to the nation's debt.

CONCLUSIONS

The monetary crisis has seriously impacted the economic, as well as the social, cultural and political life of Indonesia. The impacts of the crisis on the Indonesian economy have been severe in comparison to other countries in the region. The economic success achieved by Indonesia during 32 years of development was ruptured. Previously ranked by the World Bank with Thailand, Malaysia and other NIES (Newly Industrializing Economies), Indonesia again becomes a poor country. The impact of the crisis on social-cultural aspects of national development still persist and will require years to address.

However, this survey finds that respondents' perceptions toward the impact of the economic crisis is not completely negative. There is a satisfaction discrepancy between the way things are going now in personal life and in the country. People clearly are dissatisfied with what has been happening in the country. They share concerns about many issues, such as inflation, job security, income, crime, ethnic conflicts, and political leadership. Although they think that the country's present economic condition is bad, they believe that their personal and the country's economic situation in the near future will improve.

There are further findings that reflect dissatisfaction with social, political and economic conditions in the country. Most respondents hold the government most responsible for the total crisis, and further think that the government is in-

²⁸The National Planning Agency (Bappenas) estimated that the number of unemployed in 1998 was about 12.4 million, whereas the Ministry of Manpower estimated about 13.7 million or 15% of the nation's 93 million labor force.

competent in its response. The long-delayed recovery process has consequently affected confidence levels in social, economic and political institutions, i.e., mass media, corporations, political parties, the judiciary, and political leaders. Yet despite it all, people have managed to hold out hope for a better future.

Whether the new government of Megawati Soekarnoputri will succeed where others have failed will be determined first by internal forces—the politics of collusion, the culture of corruption—yet almost as clearly by external influences, by the developed world's reactions to and treatment of Indonesia in the short term. Indonesia cannot recover, let alone prosper, without international support and assistance.

REFERENCES

- Bisnis Indonesia*. 22 March 1997.
- Booth, Anne. 2000. "The Impact of the Indonesian Crisis on Welfare: What Do We Know Two Years On?" In Chris Manning and Peter van Diermen, eds. *Indonesia in Transition: Social Aspects of Reformasi and Crisis*. Singapore: ISEAS.
- Far Eastern Economic Review*. 4 September 1997.
- Kompas*. 5 January 1998. 'Karyawan Industri Alat Mobil Dirumahkan.'
- _____. 20 March 1998. 'Masyarakat Bawah, Korban Pertama.'
- _____. 17 April 1998. 'Dampak Krisis Moneter Lebih Parah di Pedesaan.'
- _____. 11 June 1998. 'Astra Berhenti Berproduksi.'
- _____. 29 November 1998. 'Mar'ie: Dana JPS Baru Terserap 30 Persen.'
- _____. 24 February 1999. 'JPS: Jaring Pengaman Siapa?'
- Levinsohn, James, Steven Berry, and Jed Friedman. 1999. *Impacts of the Indonesian Economic Crisis: Price Changes and the Poor*. World Wide Web document, URL: <http://www.spp.umich.edu/rsie/workingpapers/papers426-450/r446.pdf>. As accessed on 20 August 2001.
- Robison, Richard and Andrew Rosser. 1998. 'Contesting Reform: Indonesia's New Order and the IMF.' *World Development* 26, no. 8: 1593-1609.
- Soesastro, M. Hadi and M.C. Basri. 1998. 'Survey of Recent Development.' *Bulletin of Indonesian Economic Studies* 34, no. 1: 3-54.
- Sumarto, Sudarno, Anna Wetterberg, and Lant Pritchett. *The Social Impact of the Crisis in Indonesia: Results from a Nationwide Kecamatan Survey*. World Wide Web document, URL: <http://www.smeru.or.id/report/workpaper/chronicpoor/vulnerability2susenas-ref.pdf>. As accessed on 16 August 2001.
- The International Herald Tribune*. 6 November 1997.
- The Jakarta Post*. 2, 4 November 1997; 20 March 1998.
- The New York Times*. 9 January 1998.
- The Wall Street Journal*, 8, 9 January 1998.
- Thomas, Duncan, Kathleen Beegle, and Elizabeth Frankenberg (2000), *Labor Market Transitions of Men and Women During an Economic Crisis: Evidence from Indonesia*. URL: <http://www.rand.org/organization/drd/labor/DRU/DRU2344.pdf>. 16 August 2001). Presented at the conference, Social and Cultural Impacts of the East Asian Economic Crisis in Comparative Perspective, 21 September 2001, Seoul, Korea. The author thanks David Burket for his editorial assistance.

CONTRIBUTORS

BANTARTO BANDORO. Editor, The Indonesian Quarterly, CSIS, Jakarta.

JERRY W. ROWE. Forensic Accounting Consultant Mechanicville, Virginia, USA.

JUSUF WANANDI. Member, Board of Trustees, CSIS, Jakarta.

RIZAL SUKMA. Director of Studies, CSIS, Jakarta.

ROBERT ASPESLAGH. Senior Researcher, Netherlands Institute of International Relations, Clingendael.

WILLIAM E. JAMES. Senior International Economist, Nathan Associates, Inc. in the Partnership for Economic Growth (PEG) Project and PEG advisor to Bank Indonesia, Jakarta.

YASMIN SUNGKAR. Center for Political and Regional Studies, Indonesian Institute of Science (LIPI).